



Washington State Legislature

Joint Committee on Pension Policy

2001 Interim Issues

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Washington State Legislature

Joint Committee on Pension Policy

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2001 Interim Issues

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\$150,000 Death Benefit

Background:

In 1996, legislation was passed providing an additional \$150,000 duty-related death benefit to survivors of LEOFF and WSP members. The duty-related death benefit is paid only where death occurs as a result of injuries sustained in the course of employment. In 1998 this benefit was expanded to cover volunteer fire fighters and reserve police officers. Following the passage of this bill, the Governor requested that the JCPP conduct a comprehensive study of duty-related death benefits for public employees. There are about 10 duty-related deaths each biennium in the combined PERS, SERS, and TRS systems.

Committee Activity:

Presentation:

December 10, 2001

Proposal Approved:

December 10, 2001

Recommendation to Legislature:

A \$150,000 death benefit should be provided to survivors of PERS, SERS, and TRS plan members who die as a result of injuries sustained in the course of employment.

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Office of the State Actuary

\$150,000 Death Benefit

December 12, 2001

Prepared by: Robert Wm. Baker

Office of the State Actuary

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Background:

A duty-related death benefit is paid only where death occurs as a result of injuries sustained in the course of employment. There is also no time limit following the injury in which the death must result.

In 1996, the Legislature passed Engrossed Second Substitute Senate Bill 5322 (Chapter 226, Laws of 1996) which provided an additional \$150,000 duty-related death benefit to survivors of members of LEOFF and WSP.

In 1998, Senate Bill 5217 (Chapter 151, laws of 1998) extend the same \$150,000 death benefit coverage to volunteer fire fighters and reserve police officers. Following the passage of this bill, the Governor requested that the JCPP conduct a comprehensive study of duty-related death benefits for public employees. The Governor further requested that the study give consideration to providing an additional duty-death benefit to all public employees.

According to the State Actuary's experience study, there are about 10 duty-related deaths each biennium in the combined PERS, SERS, and TRS systems.

Death Benefits Available:

There are three types of government sponsored death benefits available to public employees outside of the state pension systems.

- Labor and Industries (L&I);
- Social Security;
- Federal Public Safety Officers Benefit Program;
- Employer Provided

Labor and Industries Death Benefit

Labor and Industries provides a lump sum for burial expenses together with an ongoing monthly benefit. The monthly benefit is 60% of gross wages plus 2% of gross wages for each dependent. The total monthly payment cannot exceed 120% of the state's average wage -- \$3,704 for fiscal year 2001. This benefit is not offset by the Social Security survivor benefit nor is it offset by any other government pension benefit. The benefit does cease upon remarriage.

Social Security Survivor's Benefit

Social Security is paid as a monthly benefit and is available to survivors of both duty and nonduty-related deaths. The benefit amount is based on the earnings of the person who died; the more paid into Social Security, the higher the benefit. The benefit amount is based on a percentage of the deceased's Basic Social Security benefit. The percentage will vary depending on the survivor's age and on the number of surviving dependents. The most typical situations are listed below:

- Widow or widower age 65 or older: 100%
- Widow or widower age 60-64: About 71-94%
- Widow any age with a child under age 16: 75%
- Children: 75%

In general, the Social Security survivor benefit may be reduced or stopped completely if the surviving spouse:

- Returns to work and has earnings in excess of certain limits
- Already receives a Social Security benefit
- Remarries
- No longer has a child under the age of 16

Example
Male age 45 with wages of \$40,000/yr

	Monthly	Annual
Basic Benefit Rate	\$1,311	\$15,732
Spouse under ret age	\$983	\$11,800
Child under 16	\$983	\$11,800
Family Maximum	\$2,341	\$28,100

Federal Public Safety Officers Benefits Program

The Public Safety Officers Benefit Act of 1976 provides a federal duty-death benefit for police officers and fire-fighters who die in the line of duty. This is paid as a lump sum and is available to survivors of policemen and fire fighters only. The size of this benefit does not depend on the income level of the public safety officer prior to his/her death.

1976 - \$50,000
 1988 - \$100,000 with a CPI inflator
 2001 - \$143,943

Employer Provided

Basic life insurance coverage is one of the benefits of public employment. Each State employee is covered by a standard \$15,000 life policy with an additional \$5,000 coverage for accidental death. Employees may opt for more coverage if they meet the insurability requirements of the vendor and pay the necessary premiums.

Pension Benefits

Aside from the specific death benefits mentioned above, there are also pension-related death benefits. Survivors of LEOFF 1 or WSPRS active members may receive a percent of the members salary plus additional allotments for children to a maximum of 60% of salary in both plans. The survivor of an active LEOFF 2 member may receive the member's earned retirement benefit, if they were eligible, or a refund of 150% of the member's contributions and interest; and if they were not eligible to retire, a refund of the member's contributions plus interest. Active survivor benefits in most other plans are either a refund of the member's contribution and interest if the member was not eligible to retire, or an actuarially reduced benefit if they were eligible.

Budget Language:

Even though this benefit has not passed legislative muster as a stand-alone bill, the language was included in the 2000 supplemental budget and the 2001-2003 budget. In this manner it is not a permanent benefit within the retirement chapters, but rather a temporary benefit that lasts the duration of the budget itself. The payment of a death benefit, in this instance, is treated as a sundry claim.

Budget Language in ESSB 6153.SL C007 L 01 E2

Sec. 714. DEATH BENEFIT--COMMON SCHOOLS. For the period from July 1, 2001, through June 30, 2003, a one hundred fifty thousand dollar death benefit shall be paid as a sundry claim to the estate of an employee in the common school system of the state who is killed in the course of employment. The determination of eligibility for the benefit shall be made consistent with Title 51 RCW by the department of labor and industries. The department of labor and industries shall notify the director of the department of general administration by order under RCW 51.52.050.

Sec. 715. DEATH BENEFIT--STATE AGENCIES. For the period from July 1, 2001, through June 30, 2003, a one hundred fifty thousand dollar death benefit shall be paid as a sundry claim to the estate of an employee of any state agency or higher education institution not otherwise provided a death benefit through coverage under their enrolled retirement system. The determination of eligibility for the benefit shall be made consistent with Title 51 RCW by the department of labor and industries. The department of labor and industries shall notify the director of the department of general administration by order under RCW 51.52.050.

JCPP Recommendation:

A \$150,000 death benefit should be provided to survivors of PERS, SERS, and TRS plan members who die as a result of injuries sustained in the course of employment.

Fiscal Impact:

See Fiscal Note.

FISCAL NOTE

REQUEST NO.

RESPONDING AGENCY:	CODE:	DATE:	BILL NUMBER:
Office of the State Actuary	035	12/7/01	Z-1136.1-02 Z-1143.1-02

SUMMARY:

This bill impacts the Teachers Retirement System (TRS), the Public Employees Retirement System (PERS) and the School Employees Retirement System (SERS) by providing a \$150,000 death benefit, where death occurs as a result of injuries sustained in the course of employment.

Effective Date: 90 days after session.

BACKGROUND DISCUSSION:

This benefit is currently provided in the Law Enforcement Officers and Fire Fighters Retirement System, and the Washington State Patrol Retirement System, and by PERS for security personnel of the states' ports or universities.

MEMBERS IMPACTED:

We estimate that all the 63,858 active members of TRS, the 152,261 active members of PERS, and the 47,725 active members of SERS would be affected by this bill by being provided death benefit coverage, but few would die and actually receive this benefit.

We estimate that there will be .5 eligible death in TRS, 4.0 eligible deaths in PERS and 1.2 eligible death in SERS each year, and that for a typical member impacted by this bill, the increase in benefits would be \$150,000.

FISCAL IMPACT:

Actuarial Determinations:

The bill will impact the actuarial funding of TRS, PERS and SERS differently.

The bill will impact the actuarial funding of TRS, PERS and SERS by increasing the present value of benefits payable under the System as shown below. However, the increase in benefits is insufficient to increase the required actuarial contribution rate of TRS or PERS.

The employer and employee split the cost of this benefit in plan 2, while the cost in plans 1 & 3 is paid by the employer. As members transfer to plan 3 this cost will shift from the employer/employee to the employer. For SERS 2/3 this means the employer cost will increase from slightly less than .01% to somewhat more than .01%. For PERS 2/3 this means the cost will increase from somewhat more than .00% to slightly less than .01%. Because this change depends on the number of transfers and its impact is small, it is not reflected in the budget impact below.

<i>(Dollars in Millions)</i>	System	Current	Increase	Total
Actuarial Present Value of Projected Benefits	TRS 2/3	\$ 3,826	\$ 0.5	\$3,827
The Value of the Total Commitment to all Current Members	TRS 1	10,234	0.1	10,234
	PERS 2/3	11,890	3.5	11,894
	PERS 1	12,367	0.4	12,367
	SERS 2/3	1,963	1.2	1,964
Unfunded Actuarial Accrued Liability	TRS 2/3	N/A	N/A	N/A
The Portion of the Plan 1 Liability that is Amortized until 2024	TRS 1	\$ 479	\$ 0.1	\$ 479
	PERS 2/3	N/A	N/A	N/A
	PERS 1	852	0.4	852
	SERS 2/3	N/A	N/A	N/A
Unfunded Liability (PBO)	TRS 2/3	\$ (1,596)	\$ 0.3	\$ (1,596)
The Value of the Total Commitment to all Current Members Attributable to Past Service	TRS 1	4	0.1	4
	PERS 2/3	(5,078)	2.0	(5,076)
	PERS 1	227	0.4	227
	SERS 2/3	(762)	0.7	(761)
Required Contribution Rate	TRS	2.38%	.00%	2.38%
	PERS	1.63%	.00%	1.63%
	SERS 2/3	1.22%	.01%	1.23%

Fiscal Budget Determinations:

As a result of the higher required contribution rate, the increase in funding expenditures is projected to be:

Effective September 1, 2002	
Increase in Contribution Rates:	SERS 2/3
Employee (SERS 2 only)	.01%
Employer State	.01%
Costs (in Millions):	
2002-2003	
State:	
General Fund	\$.1
Non-General Fund	0
Total State	\$.1
Local Government	\$.0

2002-2005**State:**

General Fund	\$.2
Non-General Fund	<u>0</u>
Total State	\$.2
Local Government	\$.2

2002-2027

General Fund	\$ 3.5
Non-General Fund	<u>0</u>
Total State	\$ 3.5
Local Government	\$ 3.1

STATEMENT OF DATA AND ASSUMPTIONS USED IN PREPARING THIS FISCAL NOTE:

The costs presented in this fiscal bill are based on our understanding of the bill as well as generally accepted actuarial practices including the following:

1. Costs were developed using the same membership data, methods, assets and assumptions as those used in preparing the December 31, 2000 actuarial valuation report of the Public Employees Retirement System and the June 30, 2000 actuarial valuation report of the Teachers Employees Retirement System.
2. As with the costs developed in the actuarial valuation, the emerging costs of the System will vary from those presented in the valuation report or this fiscal note to the extent that actual experience differs from that projected by the actuarial assumptions.
3. Additional assumptions used to evaluate the cost impact of the bill which were not used or disclosed in the actuarial valuation report include the following:

Based on a prior study, it is assumed that eligible deaths will occur at the rate of 0.5 per year for TRS, 3.9 per year for PERS and 1.2 per year for SERS. The deaths in PERS and SERS were split in portion of the number of members. This is equivalent to a death rate of .0026% for SERS and PERS and .0008% for TRS.

4. The analysis of this bill does not consider any other proposed changes to the system. The combined effect of several changes to the system could exceed the sum of each proposed change considered individually.
5. This fiscal note is intended for use only during the 2002 Legislative Session.
6. The funding method used for Plan 1 utilizes the Plan 2 employer/state rate as the Normal Cost and amortizes the remaining liability (UAAL) by the year 2024. Benefit increases to Plan 2 will change the UAAL in Plan 1. The cost of benefit increases to Plan 1 increases the UAAL.
7. Plan 2 utilizes the Aggregate Funding Method. The cost of Plan 2 is spread over the average working lifetime of the current active Plan 2 members.

GLOSSARY OF ACTUARIAL TERMS:

Actuarial Present Value: The value of an amount or series of amounts payable or receivable at various times, determined as of a given date by the application of a particular set of Actuarial Assumptions.

Projected Benefits: Pension benefit amounts which are expected to be paid in the taking into account such items as the effect of advancement in age and past and anticipated future compensation and service credits.

Unfunded Actuarial Accrued Liability (UAAL): The cost of Plan 1 is divided into two pieces. The Normal Cost portion is paid over the working lifetime of the Plan 1 active members. The remaining cost is called the UAAL. The UAAL is paid for by employers as a percent of the salaries of all plan 1, 2 and 3 members until the year 2024.

Pension Benefit Obligation (PBO): The portion of the Actuarial Present Value of future benefits attributable to service credit that has been earned to date(past service).

Unfunded Liability (Unfunded PBO): The excess, if any, of the Pension Benefit Obligation over the Valuation Assets. This is the portion of all benefits earned to date that are not covered by plan assets.

Age 70½ Begin Benefit

Background:

To start retirement benefits, an eligible member must separate from service and apply to the Department of Retirement Systems, regardless of age. Federal law for private plans which does not apply to the Washington State Retirement Systems requires that distribution begin at age 70½ or certain penalties or consequences may apply. For a period between 1988 and 1991 it was thought that the federal requirements applied to the state, and legislation was enacted allowing distribution at 70½ so long as the federal requirement was in place. The state law was repealed shortly after the federal law was changed. Legislators can choose to begin membership upon entering office, but once they choose to participate their decision is irrevocable.

Committee Activity:

Presentation:

November 8, 2001, Full Committee Meeting

Proposal Approved:

December 10, 2001, Full Committee Meeting

Recommendation to Legislature:

Permit vested members of PERS, SERS, and TRS to begin receipt of their retirement benefits at age 70½ without any requirement that they separate from service. Legislators and state appointed officials shall have the option of entering or leaving membership at the beginning of each term of office. If they opt out of membership, the legislator or state appointed official may apply to begin their benefit if otherwise eligible.

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Age 70½ Begin Benefit

Issue:

In order to begin receiving a retirement allowance, a member must be eligible for benefits under their plan, leave employment, and apply to the department to start their allowance. They thereby leave active membership and become a retiree. The requirement that a member separate from service exists regardless of age. Federal law requires that private plans allow members to terminate active membership and begin their benefits at age 70½ without leaving employment - a rule that does not apply to governmental plans such as the Washington State Retirement Systems. Legislators and state appointed officials can choose to begin or resume membership during any term of elected office - but the decision to begin or resume is final for the duration of their service until separation from all eligible public employment.

Background:

In 1986, the Federal Tax Reform Act included a provision amending Internal Revenue Code section 401(a)(9)(C) requiring all pension and retirement benefits to begin no later than age 70½ regardless of whether the individual remained employed. This served as an exception to the general rule that the employee must leave service before the payment of retirement benefits can begin. Individuals who did not begin receiving their pension benefits by this time were made subject to a 50 percent tax on the amount that would have been paid had they retired.

To follow the federal requirement, the Legislature changed the Judicial, Judges, LEOFF, TRS, PERS, and WSPRS systems in 1988 to allow members with more than five years of service to apply for their retirement benefit after age 70½. The change adopted by the legislature was distinct from the federal requirement in that it allowed individuals to be active members and collect service credit, and be retired and collect their benefit simultaneously. The expressed intent of the legislature was that if Congress repealed the requirement for distribution at 70½, payments made to members who never left employment and began their benefit under the provision would cease. The rule was codified as RCW 41.04.065.

Federal law was changed to exempt governmental plans, a category of plans that includes the Washington State Retirement Systems, from the requirement that distribution of benefits commences at age 70½. The state retirement systems currently remain exempt from the federal 70½ rule. RCW 41.04.065 was then repealed by the Legislature in 1991, ending the age 70½ provision.

**Vested Active Members Age 70½ or Greater
by System and Plan, 2000 Valuation**

System	Plan 1 Count	Plan 2 Count	Plan 3 Count
SERS	0	81	15
JRS	1	0	0
PERS	138	167	0
TRS	20	10	0

The 2001 Legislature increased the number of hours that retirees in PERS plan 1 and TRS plan 1 could work without facing a reduction in their benefits. All retirees are still required to separate from service for 30 days, however, or be prohibited from both receiving their benefit and returning to work.

There are at least twenty states with statutes that relate to distribution of benefits at age 70½. Almost all are concerned with the requirement that benefits begin at the later of retirement or age 70½, not that benefits begin without retirement. West Virginia is an exception to this, permitting Legislators to begin their benefits at age 70½ without leaving service.

Federal Social Security benefits work very differently. Social Security allows members to work and receive benefits at eligibility, and in some circumstances accumulate additional benefits as well. In addition, the federal program increases benefits to members who choose not to receive them between their retirement age and age 70.

Legislators and state appointed officials can choose to begin or resume membership during any term of elected office. Retired members can choose upon entering office to remain retirees and collect their benefits, or resume membership and accumulate service credit. A member may choose not to enter membership initially, and then later choose effective retroactively to the first day of the current term of office by paying the employee contributions with interest. Once the official chooses to begin or resume membership, however, that choice is irrevocable until they separate from all eligible public employment.

Possible Approaches:

Members of PERS and TRS plans 1, 2, and 3 who attain age 70½ and meet the vesting requirements for their respective plans could be given the opportunity to apply for retirement benefits to begin without requiring that they separate from service. Upon application for retirement benefits, an individual would cease active membership and no longer accumulate service credit.

Executive Committee Recommendation:

At age 70½ members of PERS, SERS, and TRS may apply to begin their retirement benefits without leaving service. Upon retirement the employee shall no longer make contributions nor receive service credit, but may work and receive their benefit without reduction of their pension. Members of the Legislature and state appointed officials shall also have the option of entering or leaving the state retirement system plans each term of office. If a legislator or state appointed official member chooses to leave the retirement systems at the beginning of a term, they may apply to begin their retirement benefits if otherwise eligible.

FISCAL NOTE

REQUEST NO.

RESPONDING AGENCY:	CODE:	DATE:	BILL NUMBER:
Office of the State Actuary	035	12/07/01	Z-1158.3/02 Z-1159.3/02

SUMMARY:

Upon attainment of age 70½, members of the Teachers' Retirement System (TRS), the School Employees' Retirement System (SERS), and the Public Employees' Retirement System (PERS) may if otherwise eligible apply for their retirement benefits to begin without leaving employment. Upon application, the retired member ceases to make contributions or receive service credit.

Legislators and officials in state elective office have the option at the beginning of each term of office to move in or out of the retirement system. If members, they make contributions and receive service credit. If not members, they may if otherwise eligible begin their retirement allowance.

Effective Date: 90 days after session.

BACKGROUND DISCUSSION:

Current law requires members of TRS, SERS, and PERS to retire before benefits begin regardless of age. This generally requires the member separate from service with their employer and apply to the Department of Retirement Systems.

MEMBERS IMPACTED:

Approximately 432 members were age 70½ and eligible to receive benefits in the 2000 Valuation of the State Retirement Systems. A small number of Legislators and certain state officials are offered optional participation.

FISCAL IMPACT:

Insufficient impact to affect the contribution rates.

COLA Report

Background:

Provided as background information.

Committee Activity:

None.

Recommendation to Legislature:

None.

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Office of the State Actuary

2001 Report on Cost-of-Living Adjustments (COLA Report)

Prepared by: Christine Masters Ryser

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Appendix A: Special Study of Plan 1 Low Benefit Annuitants	To Follow

Introduction:

The 2001 Report on Cost-of-Living Adjustments is an annual update on the economic and demographic characteristics of Plan 1 Public Employees' (PERS) and Teachers' (TRS) Retirement System annuitants. The number of Plan 1 members and the expense of funding annual benefit increases to this group in particular, elicits a natural interest from the Legislature. Primarily for comparative purposes, this report also includes information on the status of annuitants in other Washington retirement plans.

Gain-sharing is a second way benefits may be increased for members in certain retirement plans. It is conditioned on the extraordinary earnings of retirement fund investments. In 2001, no gain-sharing calculations were scheduled to occur. The results of past distributions and calculations for the scheduled 2002 gain-sharing are included in this report.

The goal of this annual report is to provide legislators and the public with a profile of current retirement benefit recipients. It also analyzes the factors that determine who receives a COLA and how the size of that increase is determined. The source of the data used is information collected and maintained by the Department of Retirement Systems. Unless otherwise indicated, data is as of July 31, 2001.

Overview:

Cost-of-Living Adjustments:

Cost-of-living adjustments (COLAs) are the element of retirement benefits which are designed to compensate for expected inflation. The state of Washington has adopted a variety of approaches to providing this benefit to retirees and their beneficiaries. Differences continue to exist in eligibility requirements and the level of income protection provided by the various designs, but in general, plans have become more uniform in recent years.

Current COLAs share four characteristics. They are:

Automatic: Not subject to legislative approval.

Permanent: COLAs are ongoing features of the plans.

Cumulative: Additional COLAs are added each year.

Compounding: The amount of COLA rises each year.

Benefit tiers developed since 1977, (Plans 2/3) include a 3% COLA design. COLAs for plans developed prior to 1977 (Plans 1) differ substantially. The original designs range from LEOFF 1 with it's full CPI COLA to PERS/TRS 1 which provided only ad hoc COLAs. No two plans had identical cost-of-living provisions.

Table #1

Plan	Members Receiving	Description	Eligibility
PERS/TRS 1	40,278 20,063	Uniform/Minimum Benefit: A flat dollar amount per month per year of service which is increased each year by 3%.	<ul style="list-style-type: none"> • Age 66 or older and retired one year. • Age 65 or younger; and benefit less than the minimum benefit \$28.33 per month per year of service, (as of 7/1/00.)
	27	Age-65: Annual increase of up to 3%, based on an increase in the CPI.	When benefit received at age 65 has lost over 40% of its purchasing power.
LEOFF 1	7,886	Annual increase in CPI; compounding. No minimum benefit provided.	Benefit in effect for at least one year.
WSP	695	Annual increase in the CPI up to 3%; compounding.	Benefit in effect for at least one year.
LEOFF/PERS/ TRS/SERS 2	9,295	Annual increase in the CPI up to 3%; compounding. No minimum benefit provided.	Benefit in effect for at least one year.
TRS/SERS 3	222	Defined benefit is increased same as Plan 2. No minimum benefit provided.	One year after defined benefit payments are initiated.

When the Uniform COLA was enacted for PERS/TRS 1 in 1995, all previous COLAS for these systems were discontinued. Members eligible for a higher benefit under the Age-65 formula continue to receive benefits calculated using that formula. There were only 27 such members in 2001.

Gain-sharing:

Unlike the automatic COLAs summarized in the table above, gain-sharing is contingent on the performance of retirement fund investments. In addition, the Legislature reserves the right to amend or repeal this benefit in the future.

Gain-sharing is implemented differently in PERS/TRS 1 and Plans 3. In Plan 1, extraordinary gains boost increases in the Uniform COLA. Plan 3 extraordinary gains are distributed as a lump sum payment to eligible active and retired members' defined contribution accounts.

Characteristics of Benefit Recipients:

Former active members comprise the majority of people receiving public retirement benefits in all Plans. A small percent of recipients are the survivors or beneficiaries of the member. "Annuitants" refers to all benefit recipients, whether former members or their survivors.

Table #2

Summary of Annuitants				
	PERS/TRS 1	LEOFF 1	WSP	Plans 2/3
Total Number	85,425	7,886	695	9,517
Average				
Current Age	72	64	63	69
Age at Retirement	60	51	53	65
Years of Service	23	22	29	12
Monthly Benefit	\$ 1,206	\$ 2,618	\$ 2,644	\$ 560
Monthly Benefit per YOS	\$ 50	\$ 138	\$ 96	\$ 46

Summary of COLA Payments:

The additional payments from all 2001 COLAs were more than \$27M over COLA payments made in 2000. Table 3 shows where additional benefits were generated based on data compiled for the 2000 valuation and 7/1/01 Uniform COLA calculation.

Table #3

2001 COLA Increases (As of 9/30/01)		
System/Plan	Recipients	Annual Payments
Plan 1		
PERS	40,003	\$ 10,201,763
TRS	19,944	6,532,956
LEOFF	7,590	8,727,791
Plan 2		
PERS	7,429	\$ 1,363,278
TRS	558	159,767
LEOFF	122	37,921
Plan 3		
TRS	113	13,595
WSP	692	627,329
Total	76,451	\$ 27,664,401

Table #4

Incremental Cost of the Uniform and Minimum COLA¹ (As of 7/01/01)		
Year	PERS/TRS Recipients	Increase in Uniform/Minimum COLA
1995	57,425	\$ 8,017,053
1996	57,577	8,358,648
1997	59,412	8,996,737
1998	59,452	9,222,350
1999	59,367	11,208,033
2000	60,008	16,056,882
2001	60,302 ²	16,761,587

¹ Assumes all recipients who receive COLA beginning July 1, continue to receive benefits through the entire fiscal year.

² Different effective dates for the data used in Tables 3 and 4 produce slight differences in the totals shown for TRS and PERS recipients.

Eligibility for Social Security Increases:

Almost all public employees are required to contribute to the federal Old Age, Survivors and Disability Insurance program – better known as Social Security. This benefit provides retirement benefits which increase at the same rate as the national Consumer Price Index (CPI). Adjustments are made each January. Retirees do not have to be retired for a certain amount of time before becoming eligible for this increase. In recent years, increases in Social Security were as follows:

Table #5

Historical Increases to Social Security Benefits						
1976-85	1986-95	1996	1997	1998	1999	2000
7.2%	3.4%	2.9%	2.1%	1.3%	2.5%	3.5%

Plan 1 COLAs:

Benefit Descriptions:

Retirees of PERS 1 and TRS 1 receive increases to their retirement benefits through the Uniform COLA. Law Enforcement and Fire Fighters' Retirement System Plan 1 (LEOFF 1) members receive adjustments based on increases in the Seattle Consumer Price Index (CPI). The focus of this section is to provide information about PERS/TRS 1 COLA recipients and non-recipients. Information about LEOFF 1 benefit increases is included at the end of this section.

- **Uniform COLA**

To be eligible for this annual adjustment, retirees must satisfy one of two criteria:

- Be age-66 or older and retired for at least one year by July 1; or
- Receive a benefit that is below the minimum threshold.

The adjustment, known as the "annual increase," is based on a flat amount per month per year of service. The annual increase for July 1, 2001 was \$1.11. At this amount, an eligible retiree with 30 years of service would have received an increase of \$33.30 per month starting July 1st. ($30 \times \$1.11 = \33.30 .)

The annual increase itself increases each year by 3%. The annual increase on July 1, 2002 will be \$1.14. ($\$1.11 \times 1.03 = \1.14 .)

The Uniform COLA may be further increased by a gain-sharing distribution in even-numbered years. Gain-sharing increases become a permanent part of the base Uniform COLA amount used to calculate future 3% increases. Graph #4 on page 10 illustrates this process.

- **Minimum Benefit COLA**

Retirees younger than age 66 may receive the Uniform COLA if their benefit falls below the minimum benefit threshold. The minimum benefit acts as a threshold or trigger for eligibility to receive the Uniform COLA.

The minimum benefit threshold is increased each July 1 by the same annual increase amount determined for the Uniform COLA. On July 1, 2001 the minimum benefit threshold was \$29.44. It will increase by \$1.14 to \$30.58 on July, 2002.

Retirees who are above the minimum threshold may become eligible for the Uniform COLA in the future if the minimum increases beyond their benefit.

- **Plan 1 Gain-sharing**

Plan 1 gain-sharing is a conditional benefit that increases the amount of the Uniform COLA when extraordinary gains occur. "Extraordinary gains" is a term defined in statute. They occur when the rate of return (ROR) on PERS/TRS 1 retirement fund investments for the previous two bienniums, (4 years) averages over 10%. The amount of each gain-sharing increase is dependent on the amount of extraordinary gains.

The gain-sharing amount is determined in odd-numbered years by applying the ROR in excess of 10%, to half the assets held on July 1st of that year. Half of the gain-sharing amount is used to provide a permanent increase in the Uniform COLA beginning in January of the following year.

All members, active and retired, realize the benefits of gain-sharing, but not simultaneously. Retired members receive an immediate increase in the Uniform COLA amount when extraordinary gains are realized. Active members realize gain-sharing benefits after retirement. At this time they become eligible for a COLA amount which has been increased by past gains.

Extraordinary gains cannot be expected on a regular basis or in predictable amounts. Gain-sharing produces highly erratic results from biennium to biennium. It is likely there will be long periods of time when no extraordinary gains occur. When they do occur, they may be very small or substantial. The gain-sharing calculations for the 1999-01 and 2001-03 bienniums illustrate this volatility.

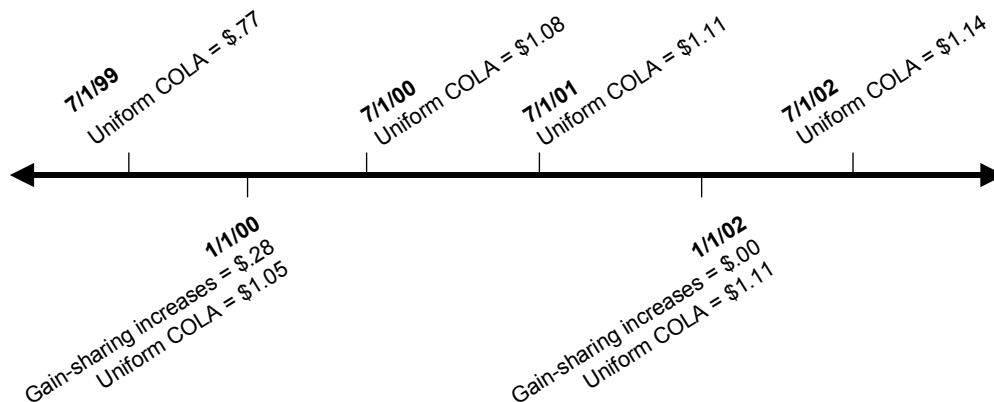
Table #6

Historical Rate of Return for PERS/TRS 1 Funds							
Biennium	1996	1997	1998	1999	2000	2001	4-year Average
1999-01	17.4%	20.5%	16.6%	11.9%	N/A	N/A	16.56%
2001-03	N/A	N/A	16.6%	11.9%	14.9%	(5.96)% ¹	8.80% ¹

¹ Best estimate as of publication.

In 1999, the gain-sharing calculation indicated that \$634 M in extraordinary returns was available to fund an increase in the Uniform COLA. This resulted in a permanent increase to the Uniform COLA of \$.28 per month per year of service in 2000. This year, the calculation indicates no extraordinary returns were realized during the previous four years. As a result, no gain-sharing increases will occur in 2002. The chart below shows the timing of Plan 1 benefit increases since 1999.

Sequence of PERS/TRS 1 Increases 1999-2002



COLA Policy for PERS/TRS 1:

Eligibility for a COLA in PERS/TRS 1 is shaped by policies implicitly and explicitly adopted by the Legislature.

The age-66 trigger for eligibility is significant for several reasons:

- It is the age when members of the Plan 2/3 systems are first eligible to retire and, after one year, (when they are 66), begin receiving the 3% COLA. The benefit provided to Plan 1 members does not start earlier than that provided to Plan 2/3 members.
- It approximates the age requirement for full Social Security benefits.
- It is considered the age when workers were most likely to permanently leave the workforce. At this point they lose the ability to replace losses in purchasing power with employment income.

In almost all of Washington's public plans COLA increases are based on a percent of benefit. The amount of the retiree's monthly benefit is multiplied by a percentage, and increases compound from year to year. This approach provides more dollars to those retirees with larger benefits. The Uniform COLA is distributed based on the member's years of service. This approach distributes the largest increases to those members who have provided the longest service.

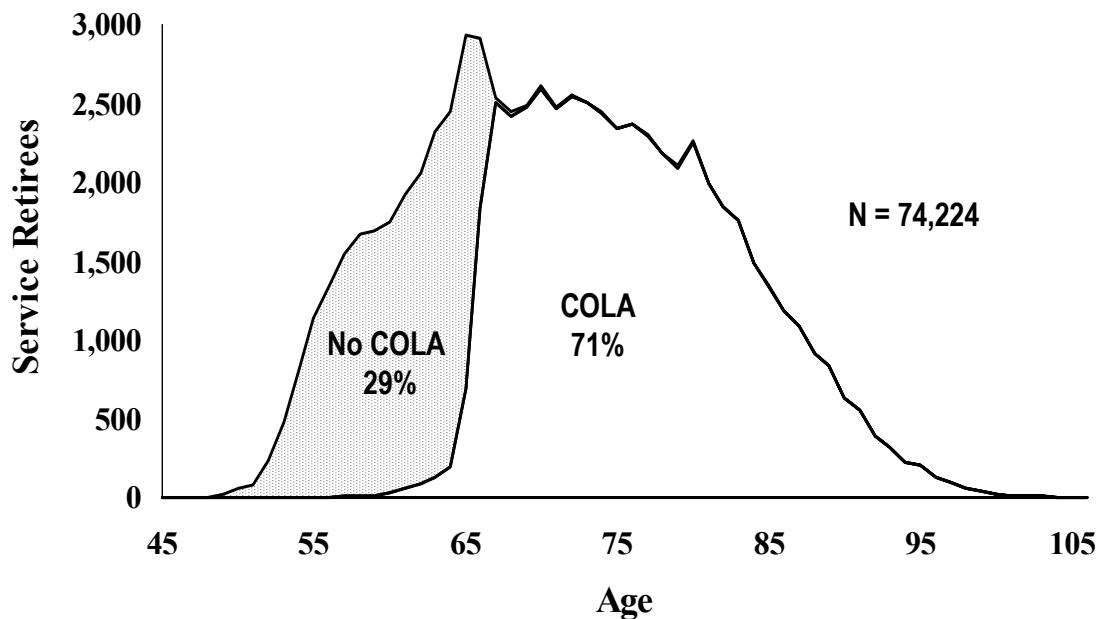
Demographics of Plan 1 Retirees:

Of the 85,425 annuitants receiving retirement benefits in PERS/TRS 1, fully 70% receive an annual cost-of-living increase. Increases for individual members were calculated on an average of 19 years of service in PERS 1 and 25 years in TRS 1. Based on the July 1, 2001 Uniform COLA amount of \$1.11, the average Plan 1 retiree saw an increase between \$21.09 and \$27.75 per month.

Table #7

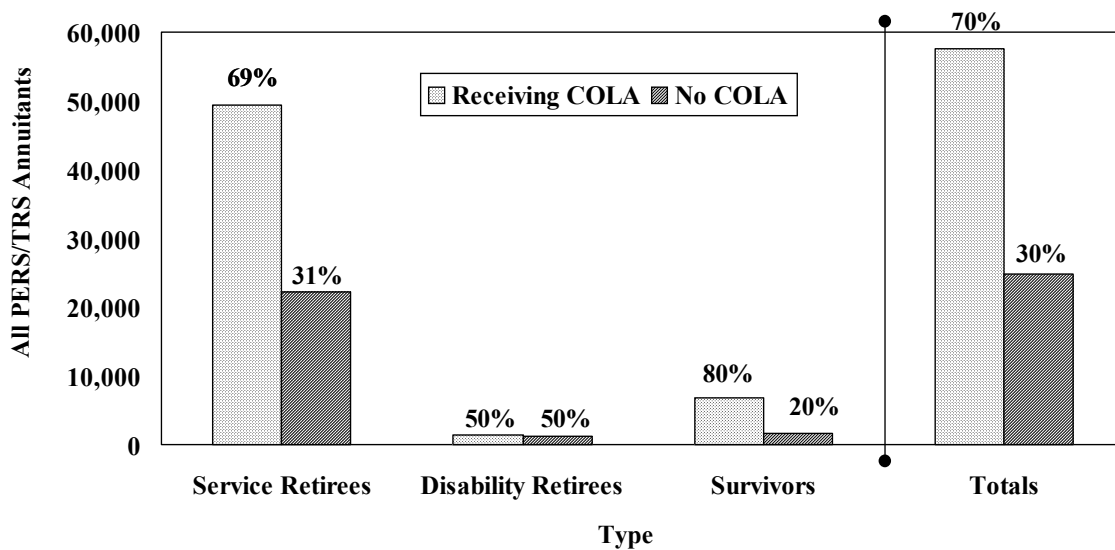
Summary of PERS/TRS 1 Annuitants				
	Receiving Uniform/Minimum		Not Receiving Uniform/Minimum	
	PERS 1	TRS 1	PERS 1	TRS 1
Total Number	40,278	20,063	13,092	11,992
Average				
Current Age	78	77	60	60
Age at Retirement	63	61	56	56
Year of Retirement	1986	1985	1997	1997
Years of Service	19	25	26	28
Monthly Benefit	\$ 843	\$ 1,144	\$ 1,844	\$ 1,837
Monthly Benefit per Year of Service	\$ 42	\$ 46	\$ 69	\$ 66

Graph #1
PERS/TRS Plan 1 COLA Status by Age



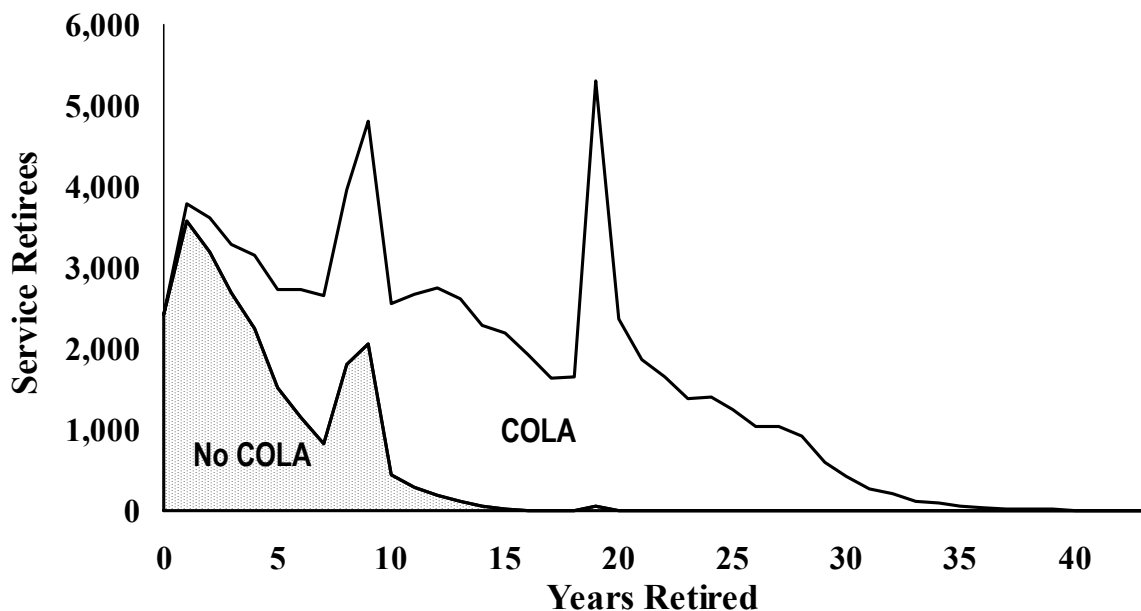
Whether an annuitant receives a COLA is largely a function of age. Almost all annuitants will eventually qualify for the Uniform COLA. Members born before July 1 and retired for at least one year, begin receiving the Uniform COLA the year they turn age-66. Members born after July 1, begin receiving the COLA the following July 1 when they are between the ages of 66.5 and 67.

Graph #2
PERS/TRS Plan 1 COLA Status by Benefit Type



Annuitants qualify for benefits under three scenarios. Most often, they are service retirees, members who have met the age and/or years of service requirements to begin receiving benefits. In other cases, they qualify as disability retirees or as the designated survivor of a retiree. Graph 2 shows the number of annuitants receiving or not receiving a Plan 1 COLA according to these three categories.

Graph #3
PERS/TRS Plan 1 COLA Status by Years Retired



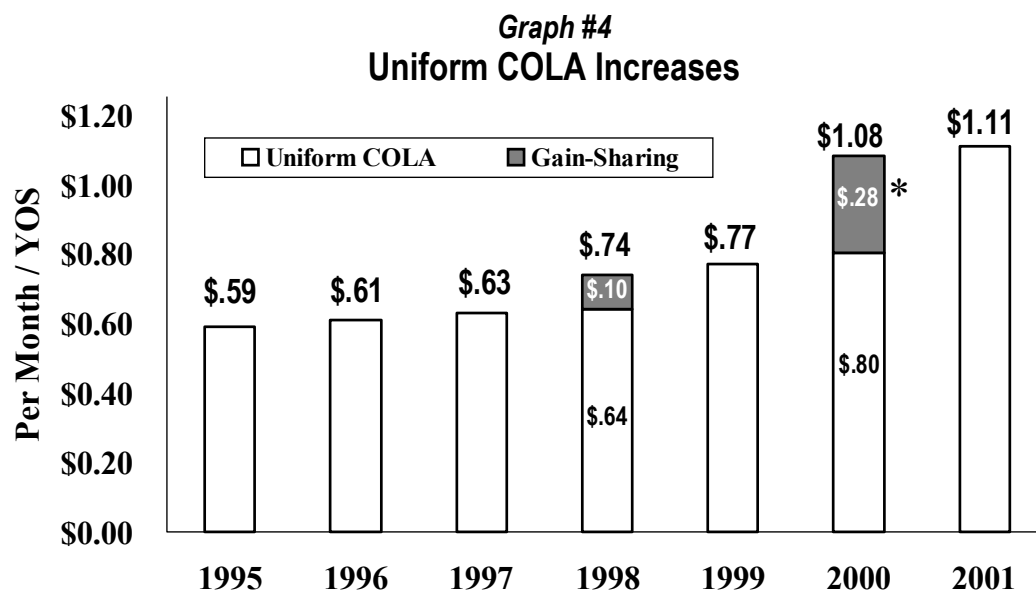
Graph 3 displays the numbers of service retirees receiving and not receiving a COLA according to how long the retiree has been retired.

The relatively early retirement provided in Plan 1 (any age with 30 YOS; 55 with 25 YOS; and age-60 with 5 YOS) means that many retirees will not qualify for a COLA in their first years of retirement. Members who have been retired the longest are most likely to be receiving a COLA. Annuitants with retirement dates prior to 1985 (16 years ago) and still not receiving a COLA are primarily beneficiaries who have not yet attained age-66.

Spikes in the graph are the results of early retirement windows offered in previous years. During those periods, unusually large numbers of members retired, some at relatively young ages. Some of these members have yet to reach COLA eligibility (age-66), even after several years of retirement.

The Uniform COLA Design:

The size of the annual increase grows each year by 3%. In even-numbered years gain-sharing may boost the COLA further. Graph #4 shows the growth of the Uniform COLA since inception and the effect the two gain-sharing distributions have had on the current level of the COLA.



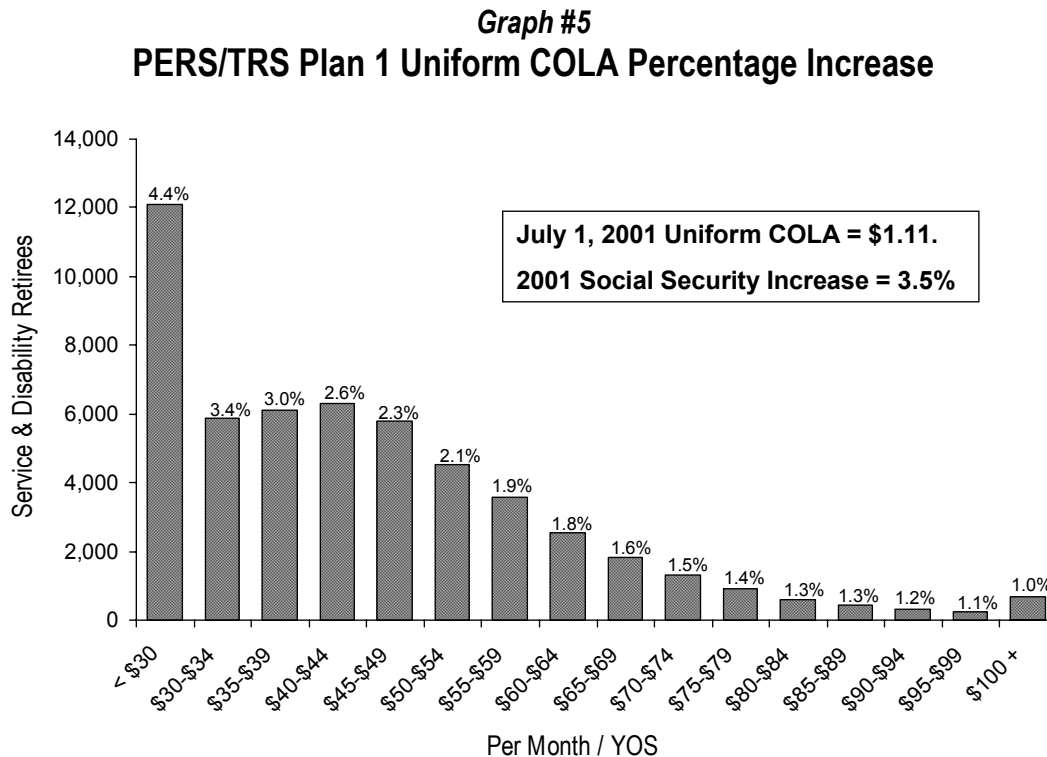
*Gain-sharing increase occurs January 1. Uniform COLA increases July 1.

Retirement benefits are based on the number of years of service and the average final salary the member earned before retirement. When looking at a member's benefit that is small it is impossible to tell whether it is small because the member had very little service credit, a low salary, or both. It is more informative to look at a retiree's benefit on a per year of service basis. For example, if a retiree receives \$800 per month and had 20 years of service, then the retiree receives \$40 per month for each of their 20 years ($\$800 \div 20 = \40 per month/YOS).

Retirees with a low benefit per year of service must have had a low salary. This could be caused by one or more of the following. The:

- Benefit was calculated using a salary from many years ago;
- Member had a low paying job; or
- Member worked part-time but received full service credit. A part-time salary with full service credit produces a benefit that is indistinguishable from a full-time person who makes a low salary.

Comparing the Uniform COLA to COLAs that provide a percentage increase is difficult. It requires that we calculate the percentage increase in the \$/month/YOS each member receives under the Uniform COLA formula. Someone who receives \$40 per month/YOS and receives the Uniform COLA increase of \$1.11 per month/YOS, recognizes a 2.6% increase in their benefit; ($\$1.11 / \$40.00 = 2.6\%$). Retirees with higher or lower benefits per month/YOS will recognize differing percentage increases.



Graph #5 demonstrates the range of percentage increases provided by the July 2000 Uniform COLA. Benefits shown have been adjusted to remove the impact of TRS annuity withdrawals and benefit payments that include survivor options.

The Uniform COLA increase distributed July 1, 2001 was \$1.11 per month/YOS. For retirees who receive a benefit less than \$30 per month/year of service, this amounted to a 4.4% increase in benefits. Retirees at the other end of the graph, who were receiving benefits of \$95 to \$99 per month/YOS saw an increase of only 1.1% in their benefits.

As a comparison, Social Security (SS) benefits increase each year by the full increase in the national Consumer Price Index (CPI). In 2000, SS benefits increased by 3.5% for all retirees. LEOFF 1 benefits are increased by changes in the CPI for Seattle. In 2000 benefits for LEOFF 1 retirees increased by 3.7%.

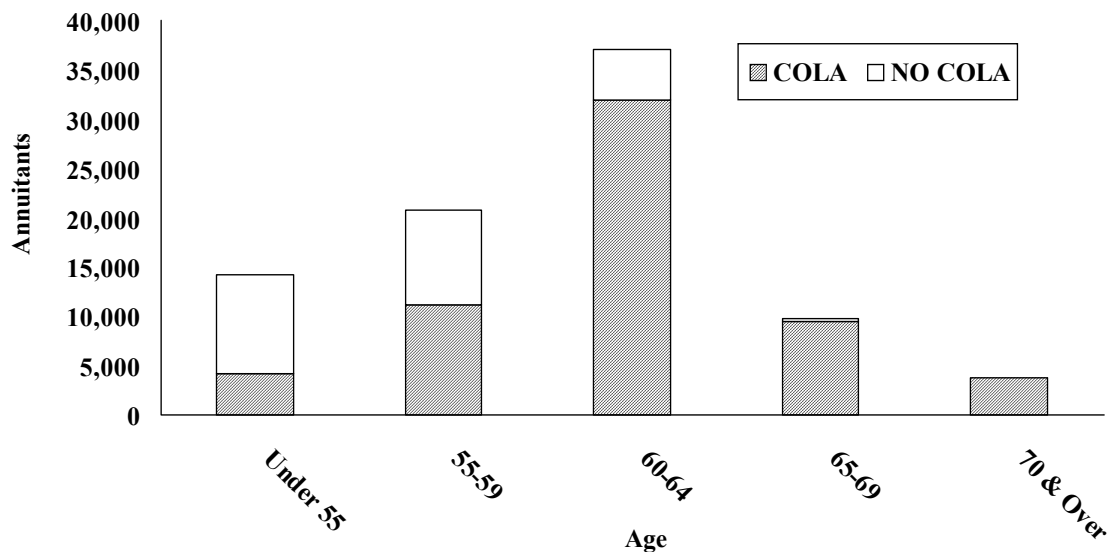
Characteristics of Plan 1 Retirees and Benefits:

As with any group of 84,000 individuals, there are both differences and similarities among its members. In understanding the impact of the Uniform COLA on PERS/TRS 1 benefits, the following variables are most useful.

Age at Retirement:

Members who retired before age-65 are less likely to be currently receiving a COLA. This is attributed to the age-66 requirement for COLA eligibility. By far, the majority of members leave employment between the ages of 60 and 65.

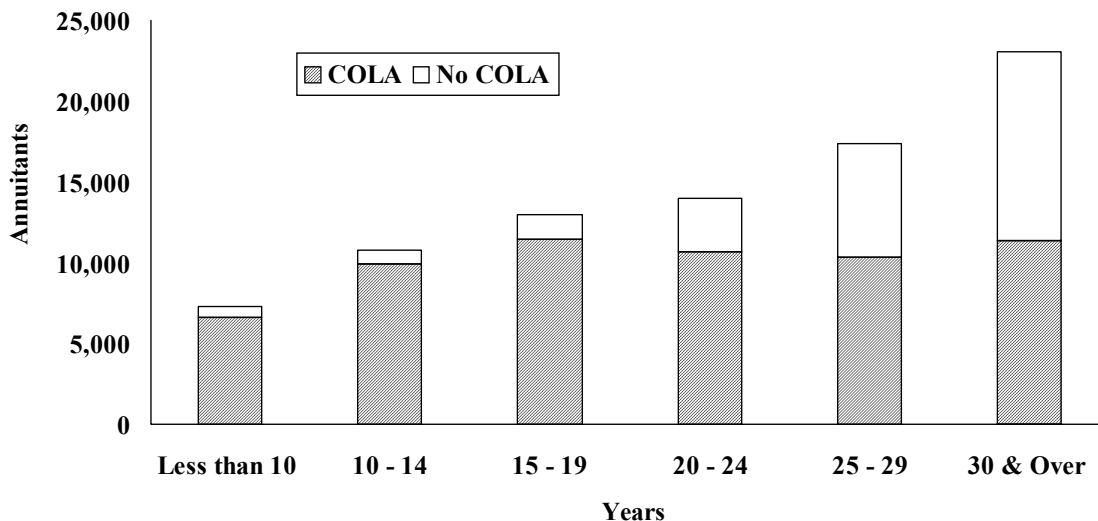
Graph #6
Member Age at Retirement



Year of Service:

PERS/TRS 1 retirement eligibility provisions allow members to retire as many as 10 years before they become eligible for a COLA. Members with over 30 years of service are eligible to retire at much younger ages. Shorter-service retirees show a higher percentage of COLA eligibility. Usually they joined the Plan at higher ages and qualified for retirement by attaining age-60 with at least 5 years of service. These members are within 6 years of COLA eligibility.

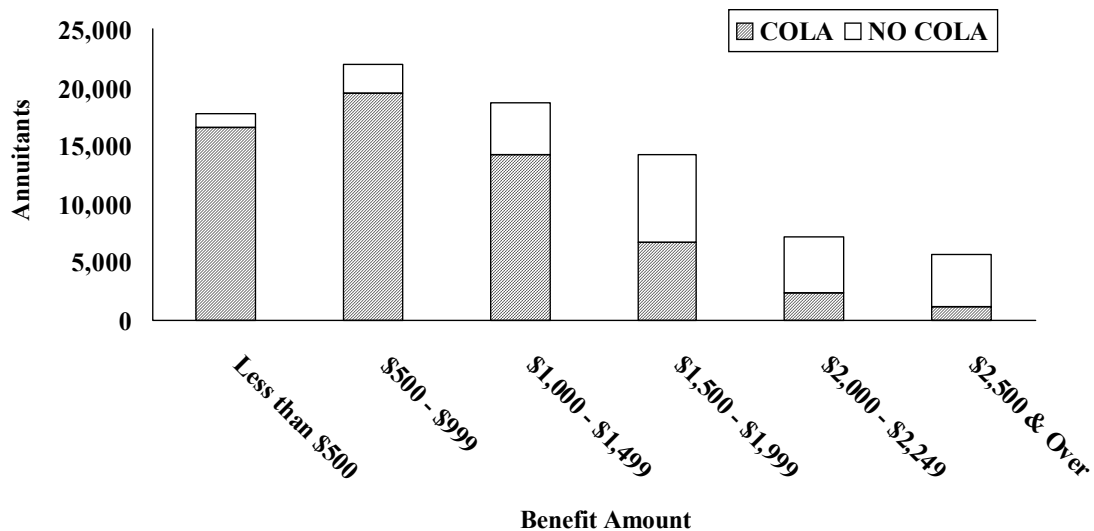
Graph #7
Years of Service



Monthly Benefit:

The distribution of monthly benefits shows a larger percentage of retirees with lower benefits receiving the COLA. This trend is influenced by two factors. Lower monthly benefits generally indicate low service or are based on salaries earned many years ago. Retirees with smaller monthly benefits are more likely to be older and thus eligible for COLA increases. Larger benefits are more likely to represent recent retirement and longer service. More recent retirees and those who retire under service eligibility tend to be younger. A smaller percent of these retirees are currently receiving COLAs.

Graph #8
Monthly Benefit



PERS/TRS 1 Minimum Benefit Recipients:

Minimum Benefit recipients form a relatively small group of Plan 1 retirees. Out of approximately 60,000 retirees receiving COLAs, only about 1,100 (2%) do so under Minimum Benefit eligibility. Members who are receiving a COLA through Minimum Benefit eligibility:

- Had an earned monthly benefit less than \$29.44 per month/YOS in 2001; and
- Are less than age-66.

In the current plan design, benefits below the Minimum Benefit threshold are increased by the annual Uniform COLA amount. The threshold acts as a trigger for Uniform COLA eligibility. As the minimum increases each year it advances on the lowest benefit levels. When a benefit level falls below the threshold, it trips eligibility for the Uniform COLA prior to age-66. These annuitants will continue to receive annual increases for the rest of their lives. At age-66, they are not longer tracked as Minimum Benefit recipients, but are counted as Uniform COLA recipients.

When the current minimum benefit design was implemented in 1995, the threshold amount was \$24.22 per month/year of service. By July of 2001, The minimum had grown to \$29.44 as a result of annual increases and periodic gain-sharing distributions.

Table #8

Summary of Minimum Benefit Recipients		
	PERS 1	TRS 1
Total Number	922	195
Average		
Current Age	62	62
Age at Retirement	55	52
Year of Retirement	1994	1992
Years of Service	17	17
Monthly Benefit	\$ 457	\$ 276
Monthly Benefit per Year of Service	\$ 26	\$ 24

LEOFF 1 COLA:

All LEOFF 1 retirees begin receiving a COLA after they have been retired for one year. In the first year they are eligible for the COLA, they also receive a retroactive increase for the first year of retirement. COLA amounts are equal to the full rise/fall in the Seattle CPI. Benefit adjustments are made April 1 of each year.

LEOFF 1 retirees and eligible spouses receive the same retirement benefits and post-retirement increases. Table 9 shows averages for all annuitants.

Table #9

Summary of LEOFF 1 Annuitants	
Total Number	7,886
Average	
Current Age	64
Age at Retirement	51
Years of Service	22
Monthly Benefit	\$ 2,618
Monthly Benefit per Year of Service	\$ 138

Table #10

Basis for LEOFF 1 COLAs Urban Wage Earners and Clerical Workers, Seattle, WA All Items, Series A					
Year	Increase	Year	Increase	Year	Increase
1986	0.71%	1991	5.53%	1996	3.30%
1987	2.35%	1992	3.54%	1997	3.10%
1988	3.35%	1993	2.98%	1998	2.63%
1989	4.68%	1994	3.66%	1999	3.10%
1990	7.11%	1995	2.90%	2000	3.75%
5-Yr. Avg.	3.64%		3.72%		3.18%

Plan 2/3 Defined Benefit COLA:

The Plans 2/3 COLA is often described as 3% a year, or up to 3% a year based on increases in the CPI. This is a generally accurate description of the actual increases members have received in the past. It is not a full description of the benefit's design.

The Plan 2/3 COLA is similar to the LEOFF 1 COLA in that each retiree is entitled to the full CPI increase from retirement. The difference is that Plan 2/3 retirees can never get an increase that is greater than 3% of the previous year's benefit. The CPI has almost always been greater than 3% and therefore, all Plan 2/3 retirees have received 3% COLAs in most years.

The size of each Plan 2/3 retiree's COLA is determined by the total amount of change in the CPI since the year they retired. Retirees of different years can receive a different COLA amount depending on the total increase in the CPI since their retirement. There is also the possibility Plan 2/3 retirees could get an increase when the CPI is negative. This would happen when the total increase in the CPI has averaged more than 3% per year since retirement.

Plan 2/3 retirees receive a COLA on the first July 1st after they have been retired one year. Plan 2/3 survivors receive the same COLA as retired members.

Plan 2/3 members need to be age-65 to receive unreduced benefits. If they retire prior to age-65 they must take an actuarially reduced benefit. The calculation of the actuarially reduced benefit includes a reduction for beginning the COLA earlier than age-66.

Plan 2 members are considered retired when they begin receiving monthly benefits. In Plan 3, a member is not considered retired for COLA purposes until they begin receiving monthly benefits from the defined benefit portion of their benefits.

Table #11

Summary of Plan 2/3 Annuitants						
	Plan 2				Plan 3	
	LEOFF¹	PERS	TRS	SERS	TRS	SERS
Total Number	169	7,680	589	126	142	38
Average						
Current Age	61	69	67	65	60	63
Age at Retirement	57	65	64	65	59	63
Years of Service	13	11	13	15	15	16
Monthly Benefit	\$ 1,003	\$ 514	\$ 812	\$ 486	\$ 346	\$ 247
Monthly Benefit per YOS	\$ 77	\$ 44	\$ 63	\$ 31	\$ 23	\$ 16

¹ LEOFF data as of 6/30/01, all others 7/31/01.

TRS Plan 3 Gain-sharing Distributions:

Plan 3 benefits include a gain-sharing benefit similar to the one administered for PERS/TRS 1 retired members. The primary differences in benefits are:

- Plan 3 gain-sharing is distributed in the form of a lump sum deposited into members' defined contribution accounts.
- Plan 3 extraordinary gains are not specifically designed as cost-of-living adjustments as they are in Plan 1. They do serve the same function of increasing the overall value of benefits.
- Retirees and actives receive the benefit of extraordinary gains at the same time.

The amount of each gain-sharing distribution is dependent on the rate of return (ROR) on defined benefit investments of plan 2/3. When the ROR for the previous two biennium averages over 10%, half of the amount over 10% is used to provide a lump sum payment to active and retired members.

The first TRS 3 gain-sharing payments were made in 1998. A second one occurred in 2000. In the future two new plans, SERS 3 and PERS 3 will also be part of the gain-sharing calculation. A gain share is calculated using all Plan 3 service earned to date. Individual members receive payments based on the gain share, multiplied by their years of service. Gain-sharing is calculated and distributed to members' defined contribution accounts in January of even-numbered years (once each biennium.)

Calculation of the 2002 Plan 3 Gain-sharing Distribution:

Rates of return were as follows for the 4 years between 1998 and 2001:

Table #12

Commingled Trust Fund Rates of Return				
<u>1998</u>	<u>1999</u>	<u>2000</u>	<u>2001</u>	<u>4-Year Average</u>
16.6%	11.9%	14.9%	(5.96)%	8.80%

Table #13

TRS 3 Gain-sharing Historical Summary					
<u>Year</u>	<u>Eligible Members</u>	<u>Average Years of Service</u>	<u>Total Dollars Distributed (In Millions)</u>	<u>Share Per YOS</u>	<u>Average Dollars to Members</u>
1998	27,243	7.8	\$ 28.4	\$ 134.43	\$ 1,042
2000	35,529	8.1	\$ 72.9	\$ 254.23	\$ 2,051
2002	N/A	N/A	\$ 0	\$ 0	\$ 0
Total			\$ 101.3		\$ 3,093

Table #14

TRS 3 Gain-sharing 2000 Distribution					
	<u>Total</u>			<u>Average</u>	
	<u>Number</u>	<u>Years of Service</u>	<u>Dollars Distributed (In Millions)</u>	<u>Years of Service</u>	<u>Dollars to Member</u>
Eligible Members					
Active	34,749	278,641	\$71	8.0	\$2,039
Retired	225	2,590	\$1	11.5	\$2,926
Term-Vested	555	5,471	\$1	9.9	\$2,507
Total	35,529	286,702	\$73	8.1	\$2,051
Ineligible Members					
Not Vested	2,257	3,474		1.5	
DC Account Balance Less Than \$1,000	3,397	1,033		0.3	
Total	5,654	4,508		0.8	

Washington State Patrol:

2001 COLA Policy:

Unlike other Washington retirement systems, the Washington State Patrol Retirement System (WSP) provides two different levels of benefits for retirees and their survivors. Originally, retirees received a benefit based on their years of service and increased each year by a simple 2% non-compounding COLA. Survivors received a benefit which was half of the member's average final salary and did not increase.

In 1999, the Legislature responded to concerns about WSP beneficiaries' loss of purchasing power by authorizing the Department of Retirement Systems to design a new retirement benefit payment option that allowed retirees to provide inflation protection to their survivors. Retirees after July 1, 2000 could choose to receive an actuarially reduced benefit which continued on to their beneficiary at the same level and included an annual 2% simple COLA.

In 2001, the WSP COLA design was altered again. Beginning July 1, 2001, both retirees and survivors receive an annual benefit increase of up to 3%, based on increases in the Consumer Price Index (CPI). This is the same COLA design used in the Plan 2/3 tiers. The new design applies to both future annuitants and those who have already begun receiving benefits.

Table #15

Summary of WSP Annuitants <i>(As of 12/31/00)</i>		
	Service Retirees	Beneficiaries
Total Number	695	104
% of total Annuitants	85%	15%
Average		
Current Age	62	71
Age at Retirement	51	
Years of Service	29	25
Monthly Benefit	\$ 2,919	\$ 1080
Monthly Benefit per Year of Service	\$ 101	\$ 68

The summary table above shows separate data for WSP retirees and beneficiaries. Compared to annuitants in all other systems (see Table #2, page 3) the average WSP beneficiary receives a benefit per month per year of service above PERS/TRS 1 and the Plans 2/3. The average monthly benefit per year of service in PERS/TRS 1 is \$50 and in the Plans 2/3 is \$46.

Defined Contribution Plans/ Freedom Plan

Background:

Defined Contribution (DC) plans, unlike Defined Benefit (DB) plans, have no guaranteed benefit at retirement. What is guaranteed is the amount contributed to the plan by the member and the employer. The retirement benefit is the accumulated contributions to the member accounts within the plan, and the financial gains resulting from the market performance of the investments in which those accumulations were placed. In contrast, the retirement benefit in a DB plan is defined, and the member must fulfill, what are in essence, contractual requirements of the plan based on salary, service and retirement age to receive that benefit.

Late in the 2000 interim there was a suggestion from committee members that the JCPP consider and study a pure defined contribution option for Washington State public employees. Some preliminary groundwork was done early in the 2001 session. This work resulted in the drafting of preliminary statutory language that would create the Washington State Pension Freedom Plan.

Committee Activity:

Presentation:

October 22, 2001 - Full Committee

Recommendation to Legislature:

None.

Staff Contact:

Robert Wm. Baker - 586-9237 - baker_bo@leg.wa.gov



Defined Contribution Plans/ Freedom Plan

Robert Wm. Baker
Senior Research Analyst

Joint Committee on Pension Policy
October 22, 2001

DC Plan Characteristics

- Fixed contribution rates
- Benefit based on market performance
- Assets held in individual accounts

% of Full-time Employees in Various Retirement Plans at Medium and Large Private Establishments

	1991	1993	1995	1997
ANY PENSION	78%	78%	80%	79%
Defined Benefit	59%	56%	52%	50%
Defined Contribution	48%	49%	55%	57%
Cash, Deferred, 401(k)	44%	43%	54%	55%

Public DC Plans

- Cities
- Counties
- Regional public utilities
- Higher Education
- SC & WV teachers & school employees
- NE & ND public employees

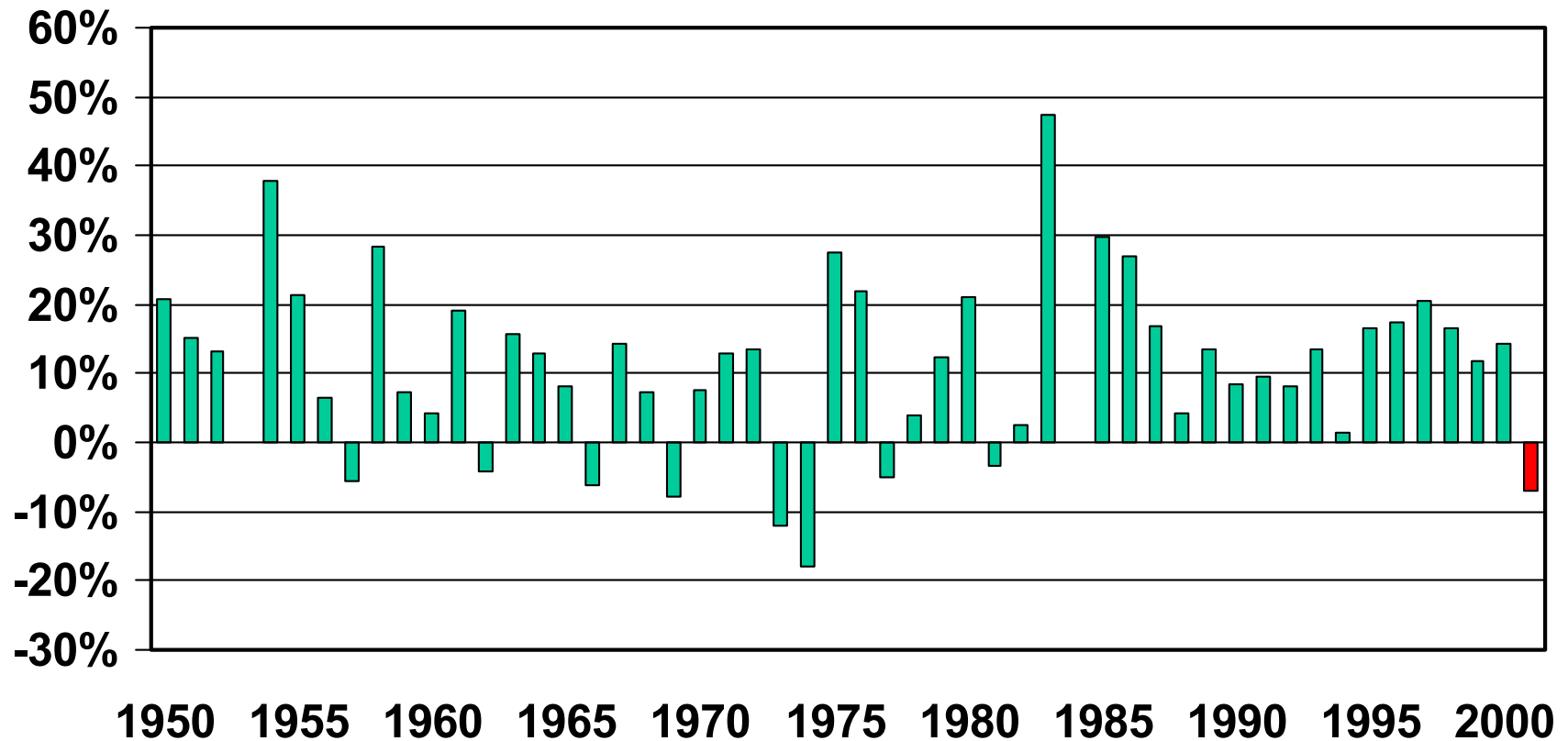
Public DC Plan Contribution Rates

	Employer	Employee
CFRTA	9.75%	5.25%
City of Lansing	6.0%	6.0%
Lackawana County	2.9%	7.5%
City of Fort Smith	10.0%	----
Nebraska State Employees	6.8 - 7.5%	4.3 - 4.8%
Northglenn General Employees	8.0%	8.0%
Northglenn Police	8.0%	12.0%

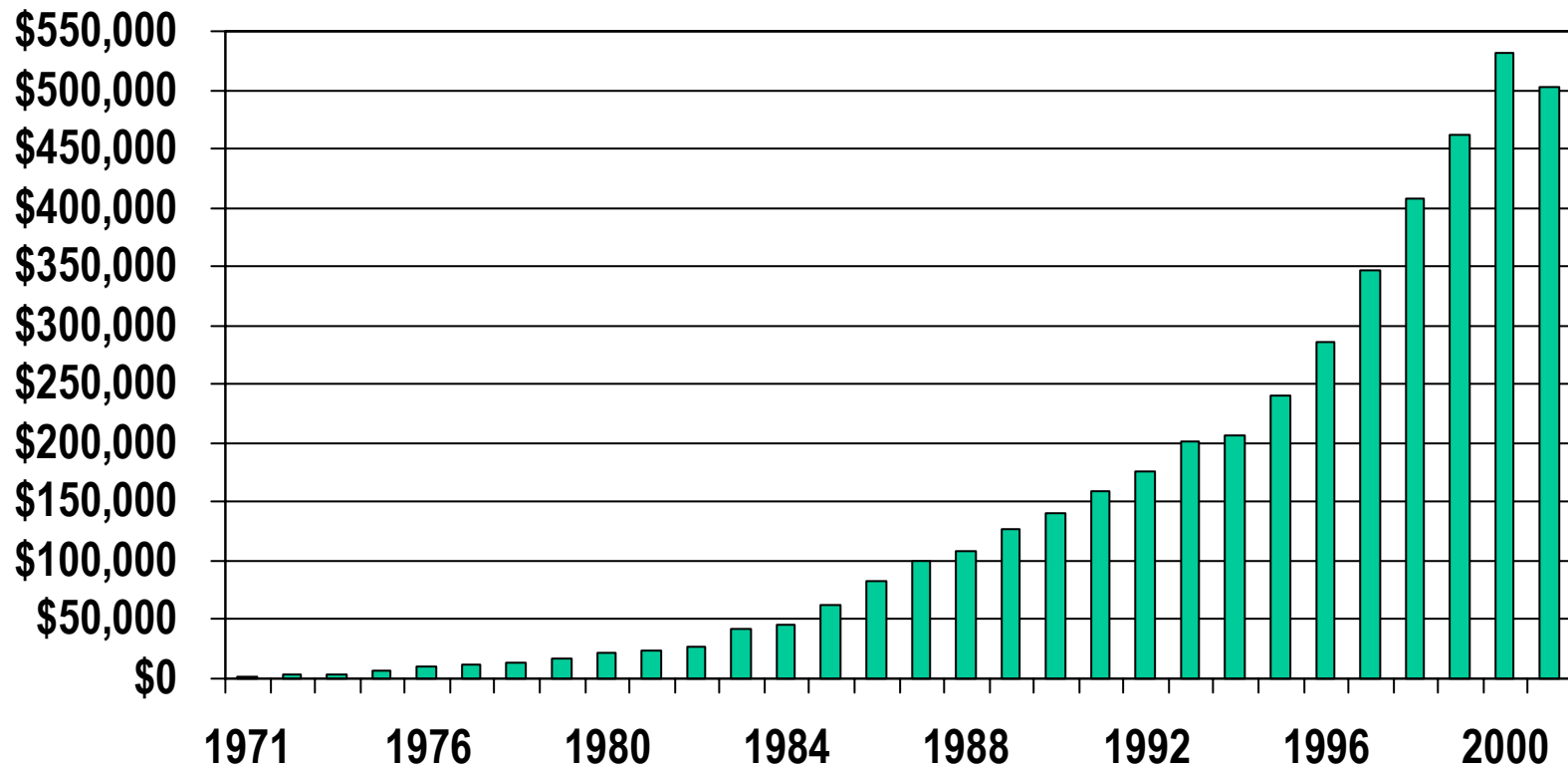
TIAA / CREF

- Higher Education faculty
- Progressive contributions
 - Up to 35 years of age: 5.0% match
 - 36 to 50 years of age: 7.5% match
 - Over 50 years of age: 10% match
- Supplemental benefit guarantee

Estimated Rate of Return on Plan Asset Mix: 1950-2001



Accumulated Total Contributions at SIB Rate of Return



Freedom Plan

- Provide additional retirement option
- Provide for employees who leave public sector before retirement
- Allow for easier career transitions
 - Immediate vesting

Freedom Plan

Contribution Rates

- 3.0% minimum to 6.0% maximum employer contribution
- Members contribution options as in Plan 3
 - 5.0%, 7.0%, 10.0%, or 15.0% of pay at all ages
 - 5.0% until 35, 6.0% until 45, 7.5% thereafter
 - 6.0% until 35, 7.5% until 45, 8.5% thereafter

Freedom Plan Investment Options

- Must select from one or more options
- May self-direct investment options similar to plan 3 except no option for SIB CTF

Freedom Plan Distribution Options

Upon termination, for any reason, the member may be paid the account balance either in a lump sum or by other options authorized by the ERBB and DRS

DC Analysis

Based on Various Contribution Rates and Rates of Return

30 th year salary		\$48,000
Total contribution rate		8.0%
Rate of return		8.0%
Total accumulation		\$178,929
Age	Annuity	% of salary
55	\$11,965	24.9%
60	\$13,337	27.8%
65	\$15,263	31.8%
PERS 2	\$27,144	56.6%

DC Analysis

Based on Various Contribution Rates and Rates of Return

30 th year salary		\$48,000
Total contribution rate		10.0%
Rate of return		8.0%
Total accumulation		\$223,662
Age	Annuity	% of salary
55	\$14,957	31.2%
60	\$16,672	34.7%
65	\$19,079	39.7%
PERS 2	\$27,144	56.6%

DC Analysis

Based on Various Contribution Rates and Rates of Return

30 th year salary		\$48,000
Total contribution rate		13.0%
Rate of return		8.0%
Total accumulation		\$290,760
Age	Annuity	% of salary
55	\$19,444	40.5%
60	\$21,673	45.2%
65	\$24,802	51.7%
PERS 2	\$27,144	56.6%

DC Analysis

Based on Various Contribution Rates and Rates of Return

30 th year salary		\$48,000
Total contribution rate		18.0%
Rate of return		8.0%
Total accumulation		\$402,591
Age	Annuity	% of salary
55	\$26,922	56.1%
60	\$30,009	62.5%
65	\$34,342	71.5%
PERS 2	\$27,144	56.6%

DC Analysis

Based on Various Contribution Rates and Rates of Return

30 th year salary		\$48,000
Total contribution rate		8.0%
SIB Rate of return		11.1%
Total accumulation		\$292,794
Age	Annuity	% of salary
55	\$19,580	40.8%
60	\$21,825	45.5%
65	\$24,976	52.0%
PERS 2	\$27,144	56.6%

DC Analysis

Based on Various Contribution Rates and Rates of Return

30 th year salary		\$48,000
Total contribution rate		10.0%
SIB Rate of return		11.1%
Total accumulation		\$365,992
Age	Annuity	% of salary
55	\$24,475	51.0%
60	\$27,281	56.8%
65	\$31,220	65.0%
PERS 2	\$27,144	56.6%

DC Analysis

Based on Various Contribution Rates and Rates of Return

30 th year salary		\$48,000
TIAA/CREF contribution rate		17.5%
TIAA/CREF Rate of return		10.7%
Total accumulation		\$596,797
Age	Annuity	% of salary
55	\$39,909	83.1%
60	\$44,485	92.7%
65	\$50,908	106.1%
PERS 2	\$27,144	56.6%

Upside

- Potential for greater benefit
- Less variance in contribution rates

Downside

- No guaranteed benefit
- No risk sharing
- More costly to administer

Who Benefits from a DC Plan

- Employers recruiting from a more mobile population
- Members who leave before reaching retirement age
- Members who stay beyond retirement eligibility

Employer's Recruitment Tool

- Labor shortage
- More likelihood of turnover
- More competition from private sector

Shorter Term Employee

- Many employees short term
- Ability to move between systems
- Ability to move between public and private

Longer Term Employees

- More in the future likely to stay beyond regular retirement age
- Benefit continues to accumulate

Governance

Background:

Pension governance is a term to describe the organizational structure by which public pensions are ordered. In many states, public pensions are governed by *retirement boards* or *boards of trustees* in which plan members have direct representation. That is different from the structure used in Washington State where pension governance functions are performed by numerous agencies and boards, as well as legislative committees.

Committee Activity:

Presentations:

September 11, 2001 - Full Committee

October 1, 2001 - Roundtable

Proposal Approved:

December 10, 2001

Recommendation to Legislature:

None.

The Joint Committee on Pension Policy adopted a motion outlining the process by which representative group input to the Joint Committee on Pension Policy may be enhanced.

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Office of the State Actuary

Governance

December 12, 2001

Prepared by: Robert Wm. Baker

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Issue:

Pension governance is a broad term used to describe the organizational structure by which public pensions are ordered. In the context of certain advocates, the term pension governance is a descriptive of a particular structure -- one in which public pensions are governed by retirement boards or boards of trustees.

Retirement boards, while common, are different than the public pension governance structure used in Washington State. In Washington, public pension governance functions are performed by numerous agencies and boards, as well as legislative committees.

Organizations representing employees and retirees have brought the issue of pension governance forward during the past several interims and legislative sessions. Often the issue is framed in criticism that the legislature does not pay these representative groups enough attention or allow them enough time to voice their issues in public hearings. The issue may, therefore, be one of process, even though representative groups have concentrated their proposals on transforming the current organizational structure governing state administered pensions in Washington State.

In addition to the requests from representative groups, the issue of pension governance was addressed in the 2001 interim because language in the State Budget (SB 6153 - C 007 L 01 E2), directed the JCPP to "... study issues of pension governance and recommend legislation for consideration in the 2002 legislative session."

Background:

As mentioned above, State administered public pensions in Washington State are governed by a collection of executive and legislative organizations that perform specific pension governance functions (see Table 1).

Table 1
Governance Functions and Responsible Agency

Pension Governance Function	Organization
Administer plans	Department of Retirement Systems (DRS)
Invest funds	State Investment Board (SIB)
Set actuarial assumptions	Pension Funding Council (PFC)
Provide for actuarial valuations	Office of the State Actuary (OSA)
Perform actuarial audits	Pension Funding Council (PFC)
Set contribution rates	Pension Funding Council (PFC)
Prepare fiscal notes	Office of the State Actuary (OSA)
Study pension issues & propose legislation	Joint Committee on Pension Policy (JCPP)

The current pension governance structure in Washington State has evolved over many years. Prior to 1976, the state's public retirement systems were under the oversight of boards of trustees. The duties of these boards were to invest the retirement funds, hire the executive director, contract for actuarial services, propose legislation to improve benefits for members and retirees, and the set contribution rates. Also prior to 1976, there existed the Public Pension Commission which oversaw the state public employees retirement system.

DRS and OSA in 1976

Then In 1976, following a period of rapid increases in pension benefits, and more rapidly escalating costs, the Legislature created the Department of Retirement Systems (DRS), with a director appointed by the Governor. This department would assume most of the oversight duties of the various retirement boards.

1976 was also the year in which the Office of the State Actuary (OSA) was created. OSA was created to provide all retirement system actuarial services for both DRS and the Legislature, including the studies used for setting contribution rates. Other duties included advising the legislature on pension issues and preparing fiscal notes for proposed legislation. OSA was established as an office in the legislative branch.

SIB in 1981

Then in 1981 the State Investment Board (SIB) was created to manage the investment of the assets of the state retirement systems. The SIB has nine voting members and four non-voting members who are investment professionals.

JCPP in 1987

In 1987 the Joint Committee on Pension Policy (JCPP) was created to study pension benefit and funding policies and issues, and to appoint or remove the state actuary by a two-thirds vote. And , of course, OSA provides staffing to the JCPP.

ERBB in 1995

In 1995 the Employee Retirement Benefits Board (ERBB) was created to oversee certain aspects of the newly created Teachers' Retirement System (TRS) Plan 3 and the state's deferred compensation program. Among these duties were to recommend optional self-directed investments in TRS and SERS 3, Recommend optional benefit payment schedules, Recommend optional self-directed investments in the Deferred Compensation Program, and Approve actuarially equivalent annuities in Plans 2/3.

The ERBB now has 12 members. 11 are appointed by the Governor to represent active and retired members of the Public Employees' Retirement System (PERS), TRS, and the new School Employees' Retirement System (SERS). The director of DRS is also a member and is chair of the board.

PFC in 1998

In 1998, the Pension Funding Council (PFC) was created to adopt the long-term economic assumptions, employer contribution rates, and provide for actuarial audits for most of the state's retirement systems. The membership of the PFC consists of the chair and ranking minority members of the Senate Ways and Means Committee and the House Appropriations Committee, and the directors of the Office of Financial Management (OFM) and DRS.

Other States

According to the most recent extracts from the PENDAT database, and some additional research, 47 States have either a Retirement Board or Board of Trustees that have one or more levels of functional authority governing one or more of the State administered retirement plans.

That may sound a bit ambiguous, but that is because there is no general rule or pattern of governance formulae from state to state. There are even instances where there is no consistent governance pattern within states. Take New York as an example: the New York State and Local Retirement System does not have a Retirement Board or Board of Trustees but the New York Teacher's Retirement System does. So with this level of variability from state to state, and even within states, averages tend to be of little value.

Here are some tabulations from the most recent PENDAT information. The PENDAT survey focused on three major aspects of governance functional authority – investments, benefit administration, and actuarial assumptions.

Table 2
Functional Authority by Plans and States

Functional Authority	Plans	States
Investments	57	31
Benefit Administration	54	30
Actuarial Assumptions	77	41

- There were 57 plans in 31 states where a retirement board had functional authority over the investment of funds,
- There were 54 plans in 30 states where a retirement board of board of trustees had functional authority over the administration of benefits,
- And, there were 77 plans in 41 states where the board or trustees had authority over the setting of actuarial assumptions.

Looking at the tabulation in a different perspective gives us an idea of the breadth of functional authority these Retirement Boards or Boards of Trustees have.

Table 3
Degrees of Functional Authority by Plans and States

Functions	Plans	States
Three	33	23
Two	42	29
One	4	3
None	4	2

- In 33 plans in 23 states the retirement board has authority over these three major functions.
- In 42 plans in 29 states the board has authority over two of the major functions.
- In 4 plans in 3 states the board has authority over one function.
- And in 4 plans in 2 states the board has no authority over any of these functions (Minnesota and New Mexico).

But relative to these functions, it appears that In no instance does any State Legislature or Assembly surrender either the authority to grant benefit increases or legislative oversight. This tends to be in keeping with the recommendations from the National Conference of State Legislators...

"...state legislatures should approve all changes of benefits and funding of retirement systems, and should regularly review their management and investment policies."

NCSL Pensions Working Group Recommendations for Policy

Legislation:

In the past 3 session there have been several governance-related bills before the legislature. One of the bills introduced during this period was sponsored by the JCPP.

HB 1771 was introduced in 1999. It would have created a Pension Oversight Board. This board would have consisted of:

- 4 active members,
- 3 retired members,
- the directors of DRS and OFM,
- the executive director of SIB, and
- 4 members of the legislature.

Their duties would have been to...

- set contribution rates,
- propose changes in policy and legislation,
- appoint or remove State Actuary, and
- discharge its duties solely in the interest of participants and beneficiaries.

This legislation would have given the Pension Oversight Board duties currently performed by the PFC and JCPP.

1999-2001 Budget Language included a section that would have created a state pension advisory committee in DRS. The committee would have been composed of active and retired members of the retirement systems, local government representatives, and the directors of OFM and DRS. The Governor vetoed the section because its work would have duplicated the work of the JCPP, and because the budget did not include adequate funding for the scope of the advisory committee's tasks.

HB 2603 was sponsored the Joint Committee on Pension Policy in the 2000 session. This bill would have also created a Pension Oversight Board. This board would have been composed of:

- 4 retiree representatives
- 5 employer representatives
- 4 active member representatives
- the directors of DRS, OFM,
- the executive director of SIB
- 4 Legislators (ex-officio)

The duties of this board would be to:

- Have an open and balanced review of pension issues,
- Recommend changes in policy, contribution rates, and long-term assumptions,
- Recommend legislation, and
- Discharge its duties in the interest of public employers, participants, and beneficiaries.

HB 2083 and HB 2185, two near-identical bills, were introduced in the most recent session. Each of these bills would have created a Washington State Pension Board. This board would have consisted of:

- 1 retired & 1 active PERS member
- 1 retired & 1 active TRS/SERS member
- 1 retired & 1 active LEOFF, WSPRS, or JRS member
- the State Treasurer
- the Director OFM
- 1 employer member
- 2 at-large members

This board would...

- Adopt actuarial assumptions,
- Set contribution rates,
- Propose legislation,
- Hire the DRS director,
- Contract for actuarial, auditing, and legal services, and
- Discharge its duties solely in the interest of the participants and beneficiaries.

This would have eliminated the PFC and, therefore, the Pension Funding work group. The board would not have been required to work with DRS, OSA, or SIB in determining economic assumptions. The OSA would no longer perform the actuarial valuations.

Other Issues:

Other Issues that should be considered when discussing governance are:

- The Large number of retirement systems: PERS 1&2; TRS 1,2,&3; SERS 2&3; LEOFF 1&2; WSPRS. How much employee representation would be required from this array of plans?
- Broad membership within these systems from entry-level to senior management including legislators.
- Then there's the basic question of Who is the Employer? In the TRS and SERS systems, the School Districts receive the majority of their operating funds from the State - does this make the State the employer?
- What would be the legal implications of declaring these plans to be TRUSTS rather than contracts? That is unclear.

Options:

1. ***HB 2083 - Create Controlling Board*** - This proposal would give representative groups more functional control. The Washington State Pension Board would have 11 members, 6 being active and retiree representatives. This board would adopt actuarial assumptions, set contribution rates, propose legislation, hire the DRS director, contract for actuarial, auditing and legal services, and eliminate the PFC.
2. ***HB 2603 - Create Advisory Boards*** - This proposal would give representative groups greater voice. The original bill would have created a Pension Oversight Board. This variation would create boards for each system (PERS, TRS etc.) comprised of employee, employer, and retiree representatives. The boards would be within DRS with the directors of DRS and OFM, plus the executive director of the SIB as members.

These boards would have an open and balanced review of pension issues; recommend changes in policy, contribution rates, and long-term assumptions; recommend legislation; and discharge their duties in the interest of public employers, participants, and beneficiaries

3. ***Enhancing Input to the JCPP*** - This proposal, based on a representative group outline, would give those groups greater voice in the development of the JCPP agenda, and give them an opportunity to build consensus on pension related priorities among themselves and JCPP members. The process would work as follows:

- The JCPP shall invite active, retiree, and employer representatives to participate in a work-group that would convene for the purpose of developing consensus on issues to be considered by the JCPP.
- The work-group would then meet with members of the JCPP Executive Committee prior to the interim to present an outline of recommended issues for consideration by the full committee.
- Issue work-groups could then be formed to work on proposed issues. These groups would include JCPP members, and OSA could provide staff assistance.

Proposal:

The Joint Committee on Pension Policy decided upon option 3. This option could be accomplished in statute, by a committee rule/resolution, or by committee motion. The executive committee voted to draft a Motion (see Appendix A).

Fiscal Impact:

None.

Appendix A

Proposed Motion for the Joint Committee on Pension Policy

To enhance representative group participation, and enable the committee to . effectively focus on pension policy issues, the executive committee of the Joint Committee on Pension Policy shall invite representatives of employee, retiree, and employer groups to participate in forming an agenda work-group. This work-group shall convene prior to the next interim to develop a proposed agenda for that interim, while recognizing the limited time and resources available. The Office of the State Actuary may provide staff support within available resources. The Chair(s) shall send a letter inviting employer, employee, and retiree groups to participate no later than the end of the first week of the legislative session.

Following the first JCPP organizational meeting, representatives of the agenda work-group shall meet with the executive committee for purposes of presenting their consensus priority list of topics and developing the interim agenda. The agenda will include issue work-groups consisting of interested participants and Joint Committee members. Recommendations from the issue work-groups shall be presented to the executive committee for inclusion in the full committee agenda no later than November.

Appendix B

Organizations with Functional Authority in Pension Governance

Pension Funding Council (RCW 41.45.100)

Members:

- Director DRS
- Director OFM
- Chair and ranking member House Appropriations Committee
- Chair and Ranking member Senate Ways and Means Committee

The PFC adopts changes to economic assumptions and contribution rates by an affirmative vote of at least four members.

Department of Retirement Systems (RCW 41.50)

- Administers all the plans.

Employee Retirement Benefits Board within DRS (RCW 41.50.086)

Members:

- 3 members each from PERS, TRS, and SERS
- 2 with experience in DC plan administration
- Director of DRS ex-officio and chair

Recommends to the SIB options for self-directed investment by plan 3 members and deferred compensation plan members. Establishes optional benefit payment schedules to members and survivors.

Joint Committee on Pension Policy (RCW 44.44)

Members:

- 8 senators – 4 majority and 4 minority.
- 8 representatives – 4 majority and 4 minority

Studies pension issues, develops pension policies, makes recommendations to the legislature.

Studies the financial condition of the pension systems, develops funding policies, and makes recommendations to the legislature.

Appoints or removes the state actuary by a 2/3rds vote of the committee.

Office of the State Actuary (RCW 44.44)

Executive is qualified in the field of actuarial science.

- Employs such research, technical, clerical personnel, and consultants as the actuary deems necessary.
- Performs all actuarial services for DRS, advises legislature and governor regarding pension benefit provisions, and funding policies and investment policies of SIB.
- Consults with the legislature and the governor concerning determination of actuarial assumptions used by DRS.
- Prepares fiscal notes on each pension bill introduced in the legislature.
- Provides actuarial services to the legislature
- Provides staff and assistance to the JCPP

State Investment Board (RCW 43.33A)

Members:

- One member each from PERS, LEOFF, and TRS
- State Treasurer
- One member each from the House and Senate
- One retiree
- Directors of L&I and DRS
- 5 nonvoting members appointed by SIB experienced in investments

The SIB has the full power to establish investment policy, develop participant investment options, and manage investment funds from the state deferred compensation program.

The SIB shall invest and manage the assets entrusted to it with reasonable care, skill, prudence, and diligence.

Legislature/ Fiscal Committees

- House Appropriations
- Senate Ways and Means

Appendix C

Historical Events in Pension Governance

(Over the past 40 years)

- 1961 -** TRS board investment decisions subject to the "prudent man" standard.
- 1963 -** State Public Pension Commission is created. Duties include:
1. To study and make recommendations regarding:
 - Financial problems of the retirement systems;
 - Amortizing the accrued liabilities of funds;
 - Extension of benefit coverage to additional public employees; and
 - Legal vesting of pension rights.
 2. Evaluate and prepare explanations for all pension proposals in terms of policy, cost implications and impact on other systems.
 3. Begin development of a standard pension policy for all state retirement systems.
- 1965 -** PERS board determines rate of interest credited to retirement funds and member contributions.
- 1969 -** Law Enforcement and Fire Fighters' Retirement System (LEOFF) established. Retirement system is administered by PERS board. Two additional members are added to PERS board. One law enforcement officer and fire fighter are each elected by their peers.
- PERS board may allocate up to 1% of investment earnings on employee contributions to provide cost-of-living adjustments (COLAs). For the first time, the board's actions are subject to the administrative procedure act.
- Investment Advisory Committee created within the State Finance Committee to recommend general investment policies, practices and procedures to the PERS and Teachers Retirement System (TRS) boards of trustees.
- 1974 -** Legislature contracts with a consultant to conduct a series of studies pertaining to retirement benefits. One study reviewed the actuarial bases of the five major Washington public employee retirement systems (PERS, TRS, LEOFF, WSP and JRS). Among its recommendations are:
1. Implementation of a consistent policy of benefit funding.
 2. Evaluation and modification of the process for determining actuarial assumptions and funding methods.
 3. Codification of funding policies and the actuarial decision-making process.
 4. Enforcement of the requirement that experience studies of the retirement systems be conducted at least every five years.
 5. Evaluation of present funding methods with particular attention to the implications of both the "rolling 40-year" amortization method used in PERS and the determination of employer contribution rates on the unfunded liabilities.

6. Analysis of the cost-of-living adjustments (COLAs) provided by excess earnings on investments, including development of long-term costs.
7. Consideration of alternative asset valuation methods to reduce volatility.

1975 - Public Pension Commission disbanded, authority remains in statute.

1976 - Department of Retirement System (DRS) created to assume trustee powers, duties and functions for all Washington retirement systems.

Boards continue to review proposed rule changes and approve applications for disability retirement. Boards cannot submit proposals to the legislature without prior evaluation by the Director and a fiscal note.

No director or board of any public retirement system may issue a written report on the assets of the system without also reporting the unfunded liability.

1976 - Office of the State Actuary is created. The actuary is appointed by a special committee of the legislature. Duties are to:

1. Perform all actuarial services for the department of retirement systems.
2. Advise the legislature and governor regarding benefits provided, funding and investment policies of the department.
3. Consult with the legislature and governor concerning determination of actuarial assumptions used by the Department.
4. Prepare a report on each pension bill introduced in the legislature explaining financial impact.
5. Provide such actuarial services to the legislature as may be required.

1977 - Plan 2 Retirement Systems created.

Prudent man standard is applied to PERS investment decisions.

1981 - State Investment Board (SIB) created. Retirement boards no longer approve investment decisions. Membership on the Investment Board is comprised of:

- One active PERS member. appointed by Governor;
- One active LEOFF member appointed by Governor;
- One active TRS member, appointed by Governor;
- State treasurer;
- One member of the House, appointed by Speaker;
- One member of the Senate, appointed by President;
- One retired member of a public retirement system, appointed by the Governor;
- Director of Labor and Industries;
- Director of DRS; and
- Five non-voting members appointed by SIB.

Duties include:

1. Investment management of 9 public retirement funds and 12 non-retirement funds. Investment must be performed in a manner that provides a maximum rate of return at a prudent level of risk.
2. Prepare quarterly and annual reports summarizing investment activities.

1982 - Individual boards for the retirement systems are abolished. The Director of DRS assumes responsibility for determining disability retirement applications.

1992 - Investment accounting duties transferred from the state Treasurer's Office to the SIB.

1998 - Pension Funding Council created.

LEOFF 2 Part-time Leave of Absence

Background:

The Law Enforcement Officers' and Fire Fighters' plan 2 contains requirements that law enforcement members be full-time, fully compensated eligible employees to remain members of the plan. LEOFF plan 2 also contains provisions for unpaid leaves of absence that may be authorized by employers. At the end of unpaid leaves of absence, members may buy up to two years of service credit totaled over their careers. Statute does not provide for an instance where a member might take a part-time leave of absence, temporarily working less than full time, for example to care for a child or loved one.

Committee Activity:

Presentation:

November 8, 2001, Full Committee Meeting

Proposal Approved:

December 10, 2001, Full Committee Meeting

Recommendation to Legislature:

Create a part-time leave of absence provision for Law Enforcement members of LEOFF plan 2, adding to existing unpaid leave of absence provisions. Upon return to full-time service, the member may purchase service credit unearned during their part-time leave within the existing two year total established for unpaid leaves of absence.

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LEOFF 2 Part-time Leave of Absence

Issue:

A law enforcement officer that is a member of Law Enforcement Officers' and Fire Fighters' Retirement System plan 2 (LEOFF 2) must remain full-time in order to maintain their membership eligibility. The LEOFF 2 statute does not clearly address part-time leaves of absence. If a member and employer want to temporarily arrange a part-time leave of absence so that, for example, a member could spend additional time caring for a child or sick parent, current rules may exclude them from LEOFF 2 for that period.

Background:

LEOFF plan 2 uses a strict set of eligibility criteria to determine membership. Generally, a person must work for an eligible employer in a full-time, fully-compensated position to be in LEOFF, among other qualifications.

Several provisions in LEOFF plan 2 permit individuals to maintain membership and receive service credit for both paid and unpaid full-time leaves of absence under several circumstances.

A member that is unpaid leave of absence authorized by their employer may receive up to two years service credit upon paying the member, employer, and state contributions to DRS within five years of returning to service. A member may also receive service credit for a paid leave of absence if they serve as an elected official of a labor organization and their employer is reimbursed by the labor organization. A member elected or appointed to a state office may elect to continue membership in LEOFF plan 2, even though they might not continue to be full time.

If an employee needs to become a part time employee for some period - for example to care for a sick relative or newborn child - they are ineligible for LEOFF membership during this period because they are not full time. Not only is the person unable to purchase their LEOFF service credit for the period of part-time employment, but could not earn any LEOFF plan 2 service credit for this period at all.

Possible Approaches:

A proposal could be created to allow for a part-time leave of absence. It could be provided to law enforcement members of LEOFF plan 2, fire fighter members, or both. In order to avoid confusion and maintain the current strict standards of LEOFF plan 2 membership, the following guidelines should be incorporated into any approach for part-time leave of absences:

1. Only allow if the individual is already a member.
2. Available for a limited duration during an individual's career.
3. Individual is prohibited from other employment with that employer during part-time leave.

Consistent with these guidelines, the following approaches might be taken:

Approach 1: Allow the member to receive proportional service credit for the amount of time worked during a part-time leave of absence. A half-time leave, for example, would enable the member to earn half service credit during that period.

Approach 2: In addition to receiving service credit for the portion of time worked, the member would have the opportunity purchase the service credit that was unearned during their part-time leave under similar terms as are provided for leaves of absence. The part-time leave periods could count proportionately towards the 2-year leave repurchase total currently allowed.

Executive Committee Proposal:

A part-time leave of absence provision for law enforcement members of LEOFF plan 2 is added to existing leave of absence rules. It is only available to existing members and has the following restrictions:

1. The part-time leave must be authorized by their employers.
2. Service credit may only be purchased for periods of part-time leave up to the existing 2-year limit.
3. Individuals are prohibited from other employment with their employer during part-time leave.

FISCAL NOTE

REQUEST NO.

RESPONDING AGENCY:	CODE:	DATE:	BILL NUMBER:
Office of the State Actuary	035	12/04/01	Z-1160.1/1161.1

SUMMARY:

Employers of the Law Enforcement Officers' and Fire Fighters' Retirement System (LEOFF) Plan 2 members may authorize a part-time leave of absence. Employees taking a part-time leave of absence remain members of LEOFF Plan 2, and upon return to full time service may purchase up to two years of service credit not earned during their part-time leave. The time purchased counts towards the existing two year limit on leaves of absence currently in statute.

Effective Date: 90 days after session.

BACKGROUND DISCUSSION:

LEOFF Plan 2 has strict requirements of full time, fully compensated service for membership. It is unclear if a member authorized to take a part-time leave of absence could remain a member of LEOFF Plan 2 for the duration of their part-time leave.

FISCAL IMPACT:

None.

PERS 1 Terminated Vested

Background:

The retirement age in PERS 1 differs depending on a member's status (active or inactive) prior to retirement. Active members with 5 years of service may receive an unreduced benefit at age 60. Inactive members, or terminated-vested members, with 5 years of service must wait until age 65 to receive an unreduced retirement benefit. This difference in retirement ages between active and inactive members does not occur in TRS 1.

Committee Activity:

Presentation:

November 8, 2001 - Full Committee

Proposal Approved:

December 10, 2001

Recommendation to Legislature:

The retirement age for inactive PERS 1 members should be prospectively reduced to 60 years of age for those who separate after attaining age 50 with at least 20 years of service.

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Office of the State Actuary

PERS 1 Terminated Vested

December 12, 2001

Prepared by: Robert Wm. Baker

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Situation Summary:

The retirement age in PERS 1 differs depending on a member's status prior to retirement. Inactive members have a higher normal retirement age than active members. This difference in retirement ages for active and inactive members does not occur in the other Plan 1 tiers, or the Plan 2 or 3 tiers.

Background:

Definitions

Inactive Member: For purposes of this report, an inactive member has the following characteristics:

- Separated from state service prior to normal retirement age;
- Vested (i.e., has at least 5 years of service); and
- Left employee contributions in the retirement system.

Active Member: For purposes of this report, an active member:

- Has not separated from service; and
- Is vested.

Retirement Eligibility

In Washington's major retirement systems, only two contain a higher retirement age eligibility for retirement from inactive status. These are the Public Employees' Retirement System Plan 1 (PERS 1) and Washington State Patrol Retirement System (WSP). The table below summarizes retirement eligibility requirements for active and inactive status.

Table 1
Retirement Eligibility Criteria

Status	PERS 1	TRS 1	PERS 2/TRS 2 TRS 3/SERS 3	WSP
Active	Age 60 and 5 YOS Age 55 and 25 YOS 30 YOS	Age 60 and 5 YOS Age 55 and 25 YOS 30 YOS	Age 65 and 5 YOS Age 55 and 20 YOS (Actuarially reduced)	Age 55 and 5 YOS 25 YOS
Inactive	Age 65 and 5 YOS Age 60 and 5 YOS (Actuarially reduced)	Same as active	Same as active	Age 60 and 5 YOS Age 55 and 5 YOS (Actuarially reduced)

Legislative History

PERS 1 Retirement Eligibility for Inactive Members:

1947 - PERS Plan 1 was created on October 1, 1947. The service retirement age was set at 60. The original statutes that created PERS 1 did not include a vested benefit provision for employees separating from service before age 60. Employees separating from service before age sixty were entitled to a return of their contributions.

1949 - Employees who involuntarily separated from service with at least 15 years of service, or at least age 50 with at least 10 years of service, were allowed to remain in membership for the exclusive purpose of receiving a retirement benefit at the age of 65. The retirement age from active service remained at age 60.

1951 - Employees who involuntarily separated from service were allowed to receive a benefit actuarially reduced from age 65 on or after attaining the age of 60. The vesting provisions established in 1949 were unchanged.

1963 - The requirement for separation to be involuntary was removed.

1965 - The years of service requirement for vesting was set at ten years of service regardless of age.

1969 - Vesting was lowered from ten years of service to five.

1996 - Eligible dual members who have PERS 1 service may receive their vested benefit prior to age 65 with no benefit reduction. Dual members are those with service in two Washington retirement systems.

TRS 1 Retirement Eligibility for Inactive Members:

1938 - TRS Plan 1 was created on April 1, 1938. As with PERS 1, the original statutes that created TRS 1 did not include a vested benefit provision. Employees separating from service, except by death or retirement, were entitled to a return of their contributions.

1947 - Employees separating from service are entitled to a return of their contributions or a deferred vested benefit at normal retirement eligibility.

Current Policy

Eligibility for unreduced retirement in the current benefit tiers was established in 1977 at age-65. In 1993, the JCPP developed additional policies regarding public employees' retirement benefits. Among them were the following statements which may be applied to the inactive retirement issue:

1. Plan design should be as neutral as possible in its effect on employees:
 - a. It should not inhibit employees from changing careers or employers.
 - b. Employees should not be encouraged to stay in jobs they consider highly stressful.
 - c. Employees should not be encouraged to seek early retirement.

2. Employees who vest and leave should be provided reasonable value toward their ultimate retirement for their length of service.

Reduction Factors

Inactive PERS 1 members have the choice of a reduced benefit between the ages of 60 and 64, or an unreduced benefit at age 65. The reduction is greater the younger the member is at retirement. The average reduction for early retirement between the ages of 60 and 65 is 8% a year (see Table 1).

Table 1
PERS 1 Reduction Factors by Age

Retirement Age	60	61	62	63	64
Reduction Factor	60%	66%	73%	81%	90%

How the Benefit Reduction Works

In the example below (Table 2), a PERS 1 and a TRS 1 member each retire from inactive status at age 60 with 10 years of service (YOS). The TRS 1 member is entitled to a benefit equal to 20% of average final compensation (AFC). The PERS 1 member is entitled to a benefit equal to 12% of AFC.

Table 2
Comparison of TRS 1 & PERS 1
Retirement Benefits For Inactive Members

System	YOS	Reduction Factor	Benefit Formula	Percent of AFC
TRS 1	10	None	2% x 10 YOS	20%
PERS 1	10	60%	2% x 10 YOS x 60%	12%

In Table 3, the percentages of AFC that were developed in Table 2 are applied to a \$30,000 AFC. Based on the given assumptions, the reduction for retiring from PERS 1 inactive status will result in a benefit \$2,400 less than the TRS 1 inactive benefit.

Table 3
Comparison of TRS 1 & PERS 1
Inactive Retirement Benefits at Age-60

	AFC		% of AFC	Benefit Amount
TRS 1	\$ 30,000	X	20%	\$ 6,000
PERS 1	\$ 30,000	X	12%	\$ 3,600

Membership Demographics

The following data (see Table 4) is provided to establish the number of members potentially affected by this issue.

Table 4
2000 Inactive PERS 1 Members By Service and Sex

YOS	Male	Female	Total
< 10	299	747	1,046
10 - 14	280	636	916
15 - 19	234	451	685
20 - 25	185	276	461
> 25	63	49	112
Total	1,061	2,159	3,220

There are currently 3,220 inactive PERS 1 members. The majority of inactive members (82%) have less than 20 years of service. Interestingly enough, while females constitute about 55 percent of all active PERS 1 members, they represent over two-thirds of Inactive members. This is likely a result of those same factors that effect women's labor force participation – child-rearing, elder-care, and spousal mobility to name the more common factors. Only in the highest service grouping did males constitute the majority of Inactive members. In addition to these current inactive members, it is anticipated that there will be approximately 3,000 future inactive PERS 1 members.

Table 5 displays the number of inactive PERS 1 retirements and the total number of PERS 1 retirements by sex for the calendar years 1996 through 2000. Active retirements in PERS 1 have increased over the past five years while inactive retirements have remained relatively stable.

Table 5
Inactive PERS 1 Retirements by Year

	Male		Female		Total	
	Active	Inactive	Active	Inactive	Active	Inactive
1996	804	62	742	92	1,546	154
1997	915	68	780	112	1,695	180
1998	928	54	844	88	1,772	141
1999	1,033	57	950	97	1,983	154
2000	1,111	50	1,009	96	2,120	146

Table 6 is a distribution of all PERS 1 retirees that have retired from inactive status by age and sex. A much higher ratio of men who are inactive members wait until they are eligible for a full retirement before taking their benefit. But even at that, the majority of inactive members take their benefit before full eligibility.

Table 6
PERS 1 Inactive Retirements by Age and Sex

Age	Male		Female	
	Number	Percent	Number	Percent
60 - 64	640	76.8%	2,151	88.1%
65 & Over	194	23.2%	289	11.9%
Total	834	100.0%	2,440	100.0%

Significance of Issue to Policy:

The PERS 1 inactive retirement age eligibility is inconsistent with current retirement benefit policies.

The other policy issue is that this delay in eligibility inhibits PERS 1 members from leaving. So pressures from PERS 1 members for early retirement legislation are more frequent than would otherwise be.

Policy Analysis:

General Observations

Legislative history gives no clues as to why PERS 1 inactive retirement eligibility remained higher than TRS 1. It may simply be the outcome of two separate retirement systems evolving in response to different administrative directions. Prior to the creation of the Plan 2 systems in 1977, there was no legislative policy for providing similar benefits for all public employees.

PERS 1 has the most restrictive policy on inactive retirements of all the major retirement systems. Outside of PERS 1 and WSP, all other state retirement plans apply the same retirement eligibility criteria regardless of members' status prior to retirement. Inactive WSP members must wait 5 years beyond the age active members can retire to receive an unreduced benefit. But retirement for active WSP members is age 55. This means WSP inactives can begin receiving a benefit at age 60. This is 5 years sooner than PERS 1 members.

In the creation of PERS 2, TRS 2, and TRS 3, the Legislature established a policy of normal retirement at age 65. The unreduced PERS 1 inactive retirement benefit is available at age 65. This provision of PERS 1, therefore, is consistent with current policy. The remaining provisions of PERS 1, however, are not

consistent with current policy. PERS 1 is the predecessor of PERS 2 and is based on retirement benefit policies in effect at the time it was created. PERS 1 has been closed to new membership since September 30, 1977.

Plan design should be as neutral as possible in its effect on employees.

PERS 1 members who wish to leave employment prior to age 60 and are not eligible for retirement may feel "handcuffed" to their job by the large reduction factor. This reduction factor provides a strong incentive for them to stay on the job until they are eligible for retirement. This incentive may discourage employees from changing careers or employers. It may also encourage employees to stay in jobs they consider highly stressful.

The inactive retirement age policy may also increase employee pressure for early retirement windows. Members who want to leave employment before they are eligible to retire are encouraged to seek an early retirement window to avoid the reduction in benefit.

Employees who vest and leave should be provided reasonable value toward their ultimate retirement for their length of service.

The reduction factor for inactive PERS 1 retirement at age 60 reduces the member's benefit by approximately 40%. This reduction substantially reduces the value of the vested benefit that would be available at age 60 had the member not separated from service.

There is also no recognition of years of service in determining the size of the reduction factor. Any member that retires at age 60 from inactive status will receive a 40% reduction in benefit regardless of how many years of service they have earned.

Alternative Approaches

1. Reduce the retirement age for inactive members to age-60.
2. Reduce the retirement age for inactive members who meet certain age and/or service requirements.
3. No change to current policy.

Approach #1 - Reduce the retirement age for inactive members to age-60.

This alternative would allow future and/or current inactive PERS 1 members to retire with an unreduced benefit based on the same eligibility requirements applied to active members:

- Age 60 with 5 YOS;
- Age 55 with 25 YOS; or
- Any age with 30 YOS.

This approach can be applicable to future inactive members only, or may include members who are currently inactive, but have not begun receiving benefits.

Considerations:

- Increases the flexibility of receiving retirement benefits for PERS 1 members. They no longer have to remain in active status to begin receiving an unreduced benefit at age 60.
- Increases the value of the vested benefit. Members who vest and terminate would be eligible for an unreduced benefit sooner.
- More consistent with current policy in other retirement system tiers.
- Lowers the unreduced PERS 1 inactive retirement age below age 65. Strictly speaking, 65 is the retirement age identified by current policy. But the Plan 1 systems were created long before this policy was implemented. The age-65 guideline may not apply in regard to the inactive retirement age.

Approach #2 - Reduce the retirement age for inactive members who meet certain age and/or service requirements.

Rather than provide a blanket eligibility for lower inactive retirement, impose certain age/ or service requirements which members must satisfy. This approach tailors eligibility to affect longer service members. As with Alternative #1, this approach can be applied to future inactives only, or current and future inactives.

Considerations:

- Increases the flexibility of receiving retirement benefits for long-service PERS 1 members. Allows longer service member more options in the case of stressful occupations, lay-offs, and career changes.
- Increases the value of the vested benefit for long service .
- More consistent with current policy on inactive retirement.
- Cost to the system is less than Alternative #1
- Lowers the unreduced PERS 1 inactive retirement age below age 65.
- Would only affect a percent of all inactives.

Approach #3 - No change to current policy.***Considerations:***

- No cost.

- Retirement eligibility for inactive members is a small part of overall benefit design. The majority of members retire from active status.

Recommendation:

The Executive Committee of the Joint Committee on Pension Policy recommends that the retirement age for inactive PERS 1 members be prospectively reduced to 60 years of age for those who separate after attaining age 50 with at least 20 years of service.

Key Features:

- Long-service employees (age-50 with at least 20 YOS) are targeted.
- Increases retirement flexibility for PERS 1 for senior-level employees who may be negatively impacted by budget cuts.
- Provides a permanent option, outside of ad hoc early retirement programs, with minimal fiscal impact.

Fiscal Impact:

See Fiscal note.

FISCAL NOTE

REQUEST NO.

RESPONDING AGENCY:	CODE:	DATE:	BILL NUMBER:
Office of the State Actuary	035	12/5/01	Z-1145.1/02 & Z-1138.1/02

SUMMARY:

This bill would impact the Public Employees Retirement System (PERS) Plan 1 by providing that future inactive members can retire with an unreduced benefit at age 60 if they separate from service after attaining age 50 with at least 20 years of service.

Effective Date: January 1, 2002.

BACKGROUND DISCUSSION:

Inactive members are those who have at least five years of service (YOS) and terminate employment without withdrawing their contributions. Currently, inactive PERS 1 members can retire with an unreduced benefit at age 65 or with a reduced benefit beginning at age 60. Active Plan 1 members can retire with unreduced benefits at or before age 60.

MEMBERS IMPACTED:

We estimate that 91 members out of the total 25,833 active members of this system would be affected by this bill.

The majority of inactive members retire at age 60, with a benefit reduced by 40% from that payable at age 65. This bill would provide these members with an unreduced benefit at age 60.

FISCAL IMPACT:

Actuarial Determinations:

The bill will impact the actuarial funding of the system by increasing the present value of benefits payable under the PERS Plan 1 and the required actuarial contribution rate as shown below:

<i>(Dollars in Millions)</i>	PERS Plan 1		
	Current	Increase	Total
Actuarial Present Value of Projected Benefits The Value of the Total Commitment to all Current Members	\$12,367	\$5	\$12,372
Unfunded Actuarial Accrued Liability The Portion of the Plan 1 Liability that is Amortized until 2024	\$852	\$5	\$857
Unfunded Liability (PBO) The Value of the Total Commitment to all Current Members Attributable to Past Service	\$11,337	\$4	\$11,341
Required Contribution Rate	1.63%	0.00%	1.63%

State Actuary's Comments:

Because the increase in the rate is less than .005% there is no immediate impact on contribution rates. The additional liability may cause the rate to round to .01% more than it would have in other years.

STATEMENT OF DATA AND ASSUMPTIONS USED IN PREPARING THIS FISCAL NOTE:

The costs presented in this fiscal bill are based on our understanding of the bill as well as generally accepted actuarial practices including the following:

1. Costs were developed using the same membership data, methods, assets and assumptions as those used in preparing the December 31, 2000 actuarial valuation report of the Public Employees Retirement System.
2. As with the costs developed in the actuarial valuation, the emerging costs of the System will vary from those presented in the valuation report or this fiscal note to the extent that actual experience differs from that projected by the actuarial assumptions.
3. Additional assumptions used to evaluate the cost impact of the bill which were not used or disclosed in the actuarial valuation report include the following: None
4. The analysis of this bill does not consider any other proposed changes to the system. The combined effect of several changes to the system could exceed the sum of each proposed change considered individually.
5. This fiscal note is intended for use only during the 2002 Legislative Session.
6. The funding method used for Plan 1 utilizes the Plan 2 employer/state rate as the Normal Cost and amortizes the remaining liability (UAAL) by the year 2024. Benefit increases to Plan 2 will change the UAAL in Plan 1. The cost of benefit increases to Plan 1 increases the UAAL.
7. Plan 2 utilizes the Aggregate Funding Method. The cost of Plan 2 is spread over the average working lifetime of the current active Plan 2 members.

GLOSSARY OF ACTUARIAL TERMS:

Actuarial Present Value: The value of an amount or series of amounts payable or receivable at various times, determined as of a given date by the application of a particular set of Actuarial Assumptions.

Projected Benefits: Pension benefit amounts which are expected to be paid in the taking into account such items as the effect of advancement in age and past and anticipated future compensation and service credits.

Unfunded Actuarial Accrued Liability (UAAL): The cost of Plan 1 is divided into two pieces. The Normal Cost portion is paid over the working lifetime of the Plan 1 active members. The remaining cost is called the UAAL. The UAAL is paid for by employers as a percent of the salaries of all plan 1, 2 and 3 members until the year 2024.

Pension Benefit Obligation (PBO): The portion of the Actuarial Present Value of future benefits attributable to service credit that has been earned to date(past service).

Unfunded Liability (Unfunded PBO): The excess, if any, of the Pension Benefit Obligation over the Valuation Assets. This is the portion of all benefits earned to date that are not covered by plan assets.

PERS 2 CVEOs to WSP

Background:

Commercial Vehicle Enforcement Officers (CVEOs) are "limited authority" officers in the WSP. In the past, they have not been commissioned officers and, as a result, members of PERS rather than WSPRS. The 2000 Supplemental Transportation Budget appropriated funds allowing up to 30 interior CVEOs to complete WSP Academy training and become commissioned troopers. As commissioned troopers, they are automatically members of WSPRS. They are currently members of both PERS and WSPRS and are eligible for a portability pension. They would like to transfer their PERS contributions and service credit into WSPRS. Because WSPRS is a more generous system than PERS, the transfer of employee and employer contributions and interest alone will not pay for the increased benefits these troopers would be eligible to receive.

Committee Activity:

Presentation:

October 22, 2001 - Full Committee

Proposal Approved:

December 10, 2001

Recommendation to Legislature:

Troopers who were commission between July 1, 2000 and June 30, 2001, after having been employed by the State Patrol as CVEOs, should be allowed to transfer their PERS 2 contributions and service credit into the WSPRS. After the transfer of employee and employer contributions plus interest, these troopers shall be responsible for all remaining required contributions such that the funding status of WSPRS remains unchanged by this transfer.

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Office of the State Actuary

PERS 2 CVEOs Transfer to WSP

December 12, 2001

Prepared by: Robert Wm. Baker

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Situation Summary:

Many groups of workers have petitioned the legislature in the hope of being granted statutory authority to transfer into a more lucrative retirement plan. Mostly it has been various "limited authority" officers desiring to be in the Law Enforcement Officers and Fire Fighters Plan 2 (LEOFF 2). This situation, with the Washington State Patrol's Commercial Vehicle Enforcement Officers is considerably different. This is a situation where the authority to chose additional training and thus membership in another plan has already been exercised. What has not been given is the statutory authority for a member to transfer their contributions and service credit from their former plan (PERS) into their current plan (WSPRS) .

The crux of this issue revolves around the transfer of retirement plan membership and service credit from one plan into another plan with better benefits. Within this issue is the question of whether that transfer is mandatory or optional, and what the costs and obligations for employees and employers are in each instance.

Background:

The Chief of the State Patrol has the authority to appoint "Special Deputies." Commercial Vehicle Officer (CVOs) and Commercial Vehicle Enforcement Officers (CVEOs), are among these. CVEOs are "limited authority" officers who have enforcement duties in the arena of commercial vehicles and school bus or private carrier buses. Because they are limited authority they are not commissioned officers and, therefore, not members of the Washington State Patrol Retirement System (WSPRS) – they are instead, members of Public Employee's Retirement System (PERS). In addition, it wasn't until recently that these officers were armed for defensive purposes. At the end of 2000 there were still 21 Commercial Vehicle Officers and 86 Commercial Vehicle Enforcement Officers in the State Patrol.

Budget Grants Authority

It was in the notations within the 2000 Supplemental Transportation Budget that authority was given for the Chief to transition up to 30 interior CVEOs into commissioned officer status and thus into the WSPRs (see Box 1). It also provided for one additional 5-month training class at the State Patrol Academy to accommodate these transition candidates, and \$181,000 was appropriated for these purposes.

These CVEOs received their State Patrol Academy training at the 85th Trooper Basic Class which began in April of 2000. Most graduated in mid-July of 2000, though a few needed some extended coaching and one required eye surgery to meet the State Patrol vision standard. The final candidate of this transitional group was commissioned on June 16, 2001.

Box 1
2000 Supplemental Transportation Budget

Agency 225
Program 010

1999-01 Revised Transportation Budget (2000 Supp)

Wednesday, March 22, 2000

**Washington State Patrol
Field Operations Bureau
Total Appropriated**

9.32 am

7. CVEO Transition - The WSP and Local 17 have entered into an agreement which provides for: 1) Transition of the 30 interior (roadside enforcement) Commercial Vehicle Enforcement positions 1's and 2's to fully commissioned Washington State Patrol officers; 2) One additional 5 month training class will be held at the Shelton Training Academy March 2000 to provide training to Commercial Vehicle Enforcement Officer (CVEO) 1's, 2's, 3's and 4's who are qualified to become commissioned officers; 3) Port of entry positions will, through attrition be filled with unarmed Commercial Vehicle Officers and up to 20 trooper cadets. (State Patrol Highway Account - State)

LEAP Committee

Current WSPRS Impact

Because there was no statutory authority to transfer contributions or service credit, there has been no impact on the WSPRS. Those CVEOs who chose to take the academy training, and transition into commissioned officer status, fall under existing pension portability rules.

Portability

Under the portability statute, a member who has membership in multiple plans could elect to retire from all the plans and receive a service retirement allowance calculated under each plan's criteria, except that the member may substitute the member's base salary from any system as the compensation use in calculating the allowances. This would mean that a CVEO who made the transition into commissioned officer status would be able to combine their PERS 2 and WSPRS service upon retirement (see Table 1).

Table 1
Portability Analysis

Assume at age 40 a PERS 2 member with 10 years of service became a commissioned officer in the WSP. They remained a commissioned officer until age 55, and attained an average final salary of \$50,000. They would then be eligible for:

$$\begin{aligned} 15 \text{ yrs} \times 2\% \text{ per year} \times \$50,000 &= \$15,000 \text{ WSPRS annual benefit immediately} \\ &\text{plus} \\ 10 \text{ yrs} \times 2\% \text{ per year} \times \$50,000 &= \$10,000 \text{ PERS 2 annual benefit at age 65} \end{aligned}$$

The member could eventually receive both parts of this benefit when they were eligible, in this case at age 65, the age at which a member is eligible to receive a full service retirement benefit in PERS 2.

Statutory Authority and Options:

So what is missing in this process is the statutory authority allowing employees the option to transfer their former membership and service credit. Typically employees in this situation have been given the options to:

- Stay in the original plan (in this case PERS),
- Change membership prospectively, in which case the members are in essence choosing a Portability retirement benefit, or
- Transfer membership, in which case they would transfer their contributions and service credit, and pay a premium based on what would have been paid into the system had they always been a member.

Since this issue involves those who've already opted to become commissioned officers, are automatically placed in the WSPRS, and are already subject to portability rules, what's left is the option to transfer contributions and service credit.

Policy:

This opens a policy question as to the transfer of contributions and service credit. In the past that policy has depended on whether the transfer between plans has been mandatory or optional:

- For a transfer that is mandatory, the policy has been that, after the transfer of employee and employer contributions (plus interest) and service credit, the employer pick up all the remaining cost.
- For a transfer that is optional, as this issue is, the policy has been that, after the transfer of employee and employer contributions (plus interest), the employee pay the cost related to the difference in employee contribution rates, and the employer pay an amount such that the transfer does not result in any change in the funding status of the plan into which they are transferring.

Successful Legislation

There have been several pieces of legislation in the last few years that have adhered to this policy. One such piece of legislation was from the 1993 session and became effective in 1994. This bill allowed police at the State's Universities and some Port Districts to be defined as "General Authority Peace Officers". Those officers were given the option of transferring into LEOFF 2, and if that option were chosen, required that appropriate payments be made.

Another similar bill that followed this policy was the legislation allowing WSU fire fighters into LEOFF 2. This was effective in January, 1996.

Other Legislation

There have been several dozen subsequent pieces of legislation that have also adhered to this policy. A representative one was introduced this last session. This bill would have defined Enforcement officers at the Department of Fish and Wildlife as "law enforcement officers" under the LEOFF chapter, and would have allowed the optional transfer of members into LEOFF 2. Again, this legislation would have required the appropriate payments from the employee and the employer.

One piece of legislation that did not adhere to the existing policy regarding transfer of membership was also introduced in the 2001 session. House bill 1610 would have allowed CVEOs and CVOs to transfer their PERS service credit and contributions with interest into WSPRS. What made this piece different from the earlier legislation, and existing policy, is that it did not require those transferring to pay the for the difference in contribution rates, and no transfer of employer contributions or difference in employer contributions was required.

Transitional CVEO Characteristics

Anytime there is a transfer of membership into a more generous plan the cost can be quite high, particularly if the policy is that there be no impact on the existing plan assets or contribution rates. Even for those with seemingly modest member service the cost may seem prohibitive. So what does the member service look like for those in this situation?

The number of CVEOs involved in this issue is quite small – less than two dozen, and their characteristics cover a very broad range (see Table 2). As you can see, their average age is less than 40 years, but the range is as high as 53 years. While their PERS member service averaged less than 10 years, several individuals had over 20 years of PERS service.

Table 2
Age and Service Credit of Transitional CVEOs

Characteristic	Average	Range
Age	38.7	28.1 - 52.9
Prior PERS Service	9.8	4.3 - 23.2

Miscellaneous Details:

- 3 with over 20 years service credit
- 2 with PERS 1 service credit
- 3 have prior PERS service credit outside WSP
- 1 under the age of 30

Adherence to existing policy has been relatively straight-forward in the more recent legislative efforts. But that policy has had well established precedent focused principally on PERS 2 members. The potential inclusion of PERS 1 members in this adds a new dimension in the arena of transfer costs, and that could require more detailed policy discussions.

Cost

Because the WSPRS offers a higher level of benefits than PERS, the transfer of employee and employer contributions and interest is not enough to pay for those benefits; additional money is needed to cover that cost. It is estimated that the total difference in just the employee contributions alone would be upwards of \$230,000 or about \$10,000 each for the 23 members (see Table 3).

Even though the average years of service is quite different between the PERS 1 and PERS 2 members, the difference between the PERS 1 and PERS 2 additional employee contributions would be relatively small. The 6% member contribution rate in PERS 1 was not that different from the 7% member contribution rate in WSPRS (while the current member contribution rate in WSPRS is 2%, it was 7% for most of the period in question.) On the other hand, the difference in contribution rates between the PERS 2 members and WSPRS members was quite significant. As a result, PERS 2 members would pay near as much in additional employee contributions as their PERS 1 counterparts; and this with only about half the average years of service.

Table 3
PERS to WSPRS Contribution Analysis by Plan

		PERS 1	PERS 2	Total
Savings Fund in PERS	Total	\$142,406	\$350,595	\$493,001
	Per Person	\$71,203	\$16,695	\$21,435
Additional Employee Contribution	Total	\$21,835	\$208,409	\$230,244
	Per Person	\$10,917	\$9,924	\$10,011
Transferred Employer Contributions	Total	\$60,205	\$350,595	\$410,800
	Per Person	\$30,103	\$16,695	\$17,861
Remaining Required Contribution	Total	\$649,975	\$966,388	\$1,616,363
	Per Person	\$324,988	\$46,018	\$70,277

Even with the transfer of employee and employer contributions plus interest, making up the difference in the total contributions could be expensive, depending on how long a member has worked. Someone who has been on the job for 20 years would be subject to 20 years difference in contribution rates plus interest. Someone working for four years would not have near as daunting a task. The average remaining required contribution for PERS 2 members would be \$46,018.

The money involved in the transfer amounts would come from the PERS funds. The remaining required contribution moneys could come from any of three sources: the employee, the employer, or the WSPRS plan surplus.

Executive Committee Proposal:

Troopers who were commissioned between July 1, 2000 and June 30, 2001, after having been employed by the State Patrol as CVEOs, should be allowed to transfer their PERS 2 contributions and service credit into the WSPRS. After the transfer of employee and employer contributions plus interest, these troopers shall be responsible for all remaining required contributions such that the funding status of WSPRS remains unchanged by this transfer.

Fiscal Impact:

None.

FISCAL NOTE

RESPONDING AGENCY:	CODE:	DATE:	REQUEST NO. BILL NUMBER:
Office of the State Actuary	035	1/7/02	Z-1137.2/02 Z-1144.2/02

SUMMARY:

This bill impacts the Public Employee Retirement System (PERS) Plan 2 and the Washington State Patrol Retirement System (WSPRS) by allowing the transfer of contributions and service credit from PERS into WSPRS. This bill is limited to commissioned troopers who were formerly employed by the Washington State Patrol (WSP) as Commercial Vehicle Enforcement Officers (CVEOs). The transfer is contingent upon each member, after the transfer of member contributions and interest and a transfer of an equal amount of employer contributions and interest, to pay all remaining costs such that the funding status of the WSPRS will not change due to this transfer.

Effective Date: 90 days after session.

BACKGROUND DISCUSSION:

CVEOs are not commissioned officers and therefore not members of WSPRS -- they are members of PERS. The 2000 supplemental transportation budget authorized academy training for up to 30 existing CVEOs. These CVEOs, having taken the academy training and been commissioned as troopers, automatically became members of the WSPRS. As a result, they are members of both PERS and WSPRS and eligible for a portability retirement.

The WSP wants to offer these particular officers the option of transferring their PERS contributions and service credit earned as CVEOs into the WSPRS. As the WSPRS offers more generous benefits than PERS, additional payments, beyond the transfer of the PERS employee and employer contributions and interest, will be necessary to pay for the cost of those benefits.

MEMBERS IMPACTED:

We estimate that less than two dozen individuals will be affected by this bill.

FISCAL IMPACT:

As the members will be responsible for the additional payments beyond the employee and employer transfer amounts, there will be no fiscal impact.

Survivor Benefits

Background:

Survivor benefits, particularly in relation to divorces, are a frequent state retirement system issue brought by constituents to the Legislature. Members divorcing before retirement may find that their survivor benefits are pre-assigned to their divorcing spouse, as this is the only available lifetime benefit available to the non-member spouse. If the member later remarries, no survivor benefit is then available for that spouse. Members divorcing after retirement find that they cannot negotiate any division of property that results in the survivor benefit being eliminated. There are also no opportunities for a divorcing non-member spouse to receive any divided benefit after the death of the member in LEOFF plan 1 or WSPRS.

Committee Activity:

Presentation:

October 22, 2001, Full Committee Meeting

Proposal Approved:

December 10, 2001, Full Committee Meeting

Recommendation to Legislature:

For future divorces, new options for dividing survivor benefits consistent with laws on community property and state divorce law are recommended.

Multiple changes are made to add flexibility to survivor benefits division, providing more options for members and divorcing spouses. Creates separate single-life benefits available in PERS, TRS, SERS and LEOFF plan 2 under most circumstances to a member and spouse divorcing before retirement. If the spouse was named as the survivor at retirement, then at divorce after retirement the entire benefit can be divided into separate single-life benefits as well. In LEOFF plan 1 and WSPRS, a spouse divorcing a member may have DRS pay them both a portion of the member's benefit, and a portion of any survivor benefit that might be created by a subsequent marriage. An optional supplemental post-retirement marriage survivor benefit is added to LEOFF plan 1 for members who choose to take an actuarial reduction during a one-year window period.

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Joint Committee on Pension Policy

Survivor Benefits

January 4, 2002

***Prepared by: David Pringle
and Robert Wm. Baker***

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Executive Summary

Statement of Situation/Problem:

Joint and survivor benefits, an important feature of many pensions, provide a continuing benefit to a survivor after the death of the member. In most plans a reduction to the member's benefit is made to fund the survivor benefit, and once the decision is made (usually at retirement) it is irrevocable.

Before retirement the pre-selection of a survivor benefit may be the only way the non-member spouse can be protected with a lifetime benefit. After retirement, there is no method to revoke the survivor benefit - even if it is the desire of both parties or the court in dividing their assets in a divorce.

Background:

There are two main types of survivor benefits featured in the various plans of the state retirement systems.

The optional, actuarial reduction-type of survivor benefit is found in the public employees' retirement system, the school employees' retirement system, the teachers' retirement system, and the law enforcement officers' and fire fighters' system plan 2. Each member's benefit is reduced to provide for their own survivor benefit. The amount of the reduction is based on the difference in the age of the member and designated survivor, as well as other plan features.

The automatic, spousal eligibility-type survivor benefit is found only in LEOFF plan 1 and the Washington State Patrol Retirement System. The benefits are paid to all spouses who meet plan eligibility criteria, and is funded through all contributions made to the plan.

The overall cost of these benefits depend on the number of survivors that qualify and the size of the benefits they receive. LEOFF plan 1 requires that the spouse be married to the member for one year prior to separation from service. WSPRS requires that the spouse be married to the member for two years prior to the member's death.

Analysis:

The purpose of the report is to define issues raised in proposing additional flexibility to survivor benefits, particularly in situations involving divorce and recognizing the importance of consistency with community property and other related state laws and policies.

Community property and divorce law principles are closely related to many survivor benefits issues. Generally, property acquired during marriage, including wages and benefits, are community property owned by both. One expression of this in state statute is the requirement in the optional plans of spousal consent to not choose less a survivor benefit at retirement. This protects the spouse's interest in the benefit.

Current law provides few avenues for revisiting the survivor benefit after the selection is made, apart from the removal of the actuarial reduction should the survivor predecease the member. The survivor benefit cannot be altered at post-retirement divorce, regardless of the wishes of the parties, though additional options to allocate pension benefits at the time of divorce could be provided.

After divorce, providing new avenues to alter the distribution of pension benefits raises many issues. The property division component of a divorce is often both a court order and contract between the divorcing spouses. State law provides procedures for creating property division arrangements, incorporating them into marriage dissolution orders, and under very limited circumstances reopening and changing them. Short of fraud, extraordinary circumstances, or manifest injustice property division agreements are rarely modified.

Willing parties might be given new avenues to correct their past mistakes, but this raises questions about creating new court proceedings or subjecting unwilling ex-spouses to further court proceedings on matters long-settled. Questions are also raised about the legislature upsetting past contracts and court decisions.

Any proposed modification of survivor benefits must consider the high risks of anti-selection associated with the issue. A member's knowledge about their life expectancy combined with unencumbered survivor choices can, if unaccounted for, lead to unexpected costs to retirement plans.

Possible Approaches:

- Optional survivor benefits could be added to LEOFF plan 1 to supplement the existing spousal-eligibility based survivor benefit for currently ineligible spouses.
- The spousal eligibility requirements for LEOFF plan 1 and/or WSPRS could be modified to include additional spouses. Some such proposals carry substantial costs.
- Separate single-life benefit options could be provided at the time of divorce. The portion of total benefits received by each spouse would not depend on the life of the other and permit the value of all benefits, including existing survivor benefits, to be divided.

JCPP Recommendation:

Different options for dividing benefits at divorce can be provided for all retirement plans. However, different approaches need to be taken in the "optional" plans and the "automatic" plans.

Approach in "optional" plans:

For PERS, TRS, SERS, LEOFF plan 2, and the future State Patrol plan the department shall adopt rules by July 1, 2003 to make a new option available at divorce - a division of the total benefits of the member and divorcing spouse into two separate single-life benefits payable for the life of that individual.

If the division occurs before the member retires, a member who later remarries will remain subject to the spousal survivor benefit requirements when they retire. Any subsequent reductions of the member's benefit shall be made solely to the member's separate benefit. The divorced spouse will be eligible to begin their single life benefit upon reaching the normal retirement age in the plan of their divorced spouse - age 60 in the plans 1 and age 65 in the plans 2.

If the division occurs after the member has retired, the separate single-life benefit option will only be available if the non-member spouse was selected as a survivor at retirement. This restriction is designed to limit anti-selection. The non-member spouse will be eligible to begin collecting their single-life benefit immediately. Members who remarry will have the option of taking a reduction to their single life benefit and select a survivor benefit for their post-retirement marriage spouse.

Separate single-life benefits are exempt from minimum benefit provisions, each may receive annual increases accounted for in the actuarial division of the benefit, and in the case of plan 3 only the member is eligible for gain-sharing payments subsequent to division into single-life benefits.

Approach in "automatic" plans:

In the "automatic" plans, LEOFF plan 1 and the current State Patrol plan, a new option for division of benefits at divorce is added permitting a divorcing spouse to receive both a portion of the member's benefit, and a portion of any eligible surviving spouse's benefit that might be created in the future. This is somewhat similar to the approach in the 2001 legislation SB 5142, but divides the existing spousal benefit rather than create an additional benefit for the life of the divorcing spouse.

In LEOFF plan 1 there is no survivor benefit available for spouses who marry members who have already separated from service. The proposal incorporates the approach of SB 5144, adding an optional, actuarially-reduced survivor benefit during a window beginning one year after a post-retirement marriage.

Statement of the Situation/Problem:

A joint and survivor benefit is a feature of many retirees' pensions. The joint and survivor benefit provides a continuing payment for the lifetime of the retiree's beneficiary following the retiree's death. The decision to select a survivor option must be made at the time of retirement. This decision is irrevocable, although in some limited circumstances a member can return to work, "re-retire" and make a new decision regarding their beneficiary designation or choice of survivor option.

When members or retirees divorce, the irrevocable survivor benefit presents several problems. Before retirement, the only benefit that a non-member spouse can be certain to receive until their death is the survivor benefit. As a result, the non-member spouse may seek to have the survivor benefit pre-assigned to them in a pre-retirement divorce. This leaves the member no ability to cover a subsequent spouse with a survivor benefit.

After retirement, a member and divorcing spouse may not revoke the survivor benefit chosen at retirement, regardless of their (or their court's) decision about how to divide their property. This can result in ex-spouses having benefits that remain dependent on each other's lives, even if they have separated in every other possible way.

Life expectancies have increased substantially in the last several decades. A person who retires at age 65 today can look forward to some twenty years of pension benefits. This increase in the span of retirement also increases the likelihood that a retiree's post-retirement financial and family needs will change due to the death of a spouse, divorce or marriage.

Background

Optional, actuarially reduced survivor benefits

Members of PERS, TRS, LEOFF Plan 2 and JRS have the option to include joint and survivor coverage as part of their pension when they retire. This option includes the flexibility to name a beneficiary other than their spouse and the opportunity to select the amount of continuing benefit for their beneficiary from among several options. But if these members do elect a survivor benefit, their monthly pension is reduced to pay for the benefit.

Typically, the beneficiary is the retiree's spouse or child. If the retiree is married and the retiree selects an option which does not provide a survivor benefit for the spouse, the spouse must consent to the retiree's choice in writing.

The choices available to the retiree for the amount of the continuing benefit paid to their beneficiary include: the full amount of the member's monthly benefit, two-thirds of the member's benefit, or one-half of the member's benefit. The following table illustrates the rate of selection of the available survivor options since 1996, when the joint and two-thirds survivor option first became available:

Table 1
Share of Retirees by Payment Options

Source: OSA

System/Plan	Single Life	Full Survivor	½ Survivor	⅔ Survivor
TRS 1	63%	20%	14%	3%
PERS 1	67%	14%	13%	6%

The continuing benefit is paid for by a reduction in the amount of the member's monthly retirement allowance. The amount of the reduction in the member's monthly retirement allowance is based on three things:

- The amount of the continuing benefit paid to the member's beneficiary;
- The member's retirement system and plan; and,
- The age difference between the member and their beneficiary.

Table 2
Example: Joint and Survivor Optional Payment Calculations

Retirement Benefit × Joint and Survivor Option Factor = Joint Benefit

Joint Benefit × Survivor Option % = Survivor Benefit

For a LEOFF 2 member with a \$30,000 retirement benefit who wishes to provide a 50% survivor benefit for a spouse who is 3 years younger, the calculation for the joint benefit would be:

$$\$30,000 \times .858 = \$25,740$$

The calculation for the survivor benefit would be:

$$\$25,740 \times 50\% = \$12,870$$

Benefit Options

In Washington State, the joint and survivor benefits for state-administered retirement plans are calculated as either a 100%, 66.7%, or 50% benefit. This means that if a member chooses a 100% Joint and survivor option, they would receive an actuarially reduced retirement benefit that, after their death, the spouse would continue receiving (see Table 3). If the member and their spouse chose a 66.7% joint and survivor option, the actuarial reduction to the retirement benefit would be less, and, after the member's death, the spouse would continue receiving a benefit at 66.7% of the joint amount. If the member and their spouse chose a 50% joint and survivor option, the actuarial reduction would be still less and, after the member's death, the spouse would continue receiving a benefit at 50% of the joint amount.

Table 3
LEOFF 2 Joint and Survivor Benefit Options
Based on a \$30,000 Allowance and 3 Year Spouse Age Difference
Source: OSA

Joint and Survivor Option	Option Factor	Joint Benefit	Reduction Amount	Survivor Benefit
100.0%	.751	\$22,530	-\$7,470	\$22,530
66.7%	.820	\$24,600	-\$5,400	\$16,408
50.0%	.858	\$25,740	-\$4,260	\$12,870

Joint and Survivor Factors

The joint and survivor factors are actuarially determined based on the average mortality experience of plan members and their designees. Generally, the greater the difference in ages, with the plan member being the older of the two, the greater the joint and survivor reduction. Even in the event that the designated survivor is significantly older than the plan member, there is still a reduction of retirement benefits.

To illustrate how age, or more specifically age differential, weighs on these payment options, consider the following situations. In the first is a retiree with a younger spouse. He has a relatively fixed period to "pay" for a survivor option that will likely be of long duration. As a result, the "payment" will be expensive, and the current retirement allowance will be reduced significantly. As shown in the first row of Table 4, a member providing a 100% survivor benefit for a spouse who is ten years younger, would see their \$2,500 monthly benefit reduced to \$1,750. Or if they wished to provide a 50% survivor benefit, the allowance would be reduced to \$2,060.

Table 4
Joint and Survivor Option Factor Analysis
Source: Washington State LEOFF 2 Options

Spouse Age Difference	Joint and 100% Factor	Adjusted \$2,500 Benefit	Joint and 50% Factor	Adjusted \$2,500 Benefit
Ten Years Younger	.700	\$1,750	.824	\$2,060
Same Age	.780	\$1,950	.877	\$2,193
Ten Years Older	.861	\$2,153	.926	\$2,315

In an alternative situation, a retiree may wish to provide a survivor benefit for an older spouse. The member will have the same amount of time to pay for a benefit that will likely be of shorter duration; as a result, the payment will be less expensive, and the retirement allowance will be reduced a lesser amount. As illustrated in the second row in Table 4, a member providing a 100% survivor benefit for a spouse who is ten years older would see their \$2,500 benefit reduced to \$2,153. Or if they wanted to provide a 50% survivor benefit, their allowance would be reduced to \$2,315.

Other States

Though joint and survivor optional payments are near universal, the details can vary from state to state. The above analysis was done using joint and survivor option factors from Washington to illustrate how a member's and their spouses' age difference can play a significant part in the joint and survivor dynamic. In Missouri, by comparison, the joint and survivor option factors are based on single year differences of the member and their spouse (see Table 5). The joint and survivor option factors used in Maryland have similar construction – single year steps for both member and beneficiary.

Table 5
Joint and Survivor 100% Option Factors
By Age of Member and Beneficiary
Source: Missouri State Employees Retirement System

Spouse Age Difference		Member Retirement Age				
		58	59	60	61	62
Years Older	2	0.856	0.852	0.848	0.844	0.840
	1	0.851	0.847	0.843	0.839	0.835
	0	0.846	0.842	0.838	0.834	0.830
Years Younger	1	0.841	0.837	0.833	0.829	0.825
	2	0.836	0.832	0.828	0.824	0.820

In comparison, while Missouri and Maryland use single year increments for both the member and the beneficiary, California uses single year increments for the member but 5-year age groupings for the beneficiaries (see Table 6.) As a result, the tabulations are simplified, though it is uncertain that the administration of the payment options is also simplified. As long as comparisons need to be made, one could argue that the single year determinations would be easier than placing the beneficiary in any particular age group. In addition, as the administration of these plans and options has become more automated, the determination of the appropriate option factor is more a matter of key-strokes than flipping pages in an optional payment manual.

Table 6
Joint and Survivor 100% Option Factors
By Age of Member and Beneficiary
Source: CALPERS

Spouse Age Difference		Member Retirement Age				
		58	59	60	61	62
Years older	10 - 14	0.927	0.925	0.924	0.923	0.921
	5 - 9	0.900	0.897	0.894	0.892	0.889
	Within 5 years	0.860	0.856	0.850	0.844	0.839
Years younger	5 - 9	0.822	0.815	0.808	0.800	0.793
	10 - 14	0.798	0.790	0.782	0.773	0.764

Washington Factors Also Simplified

Another example of a simplified approach to determining these payment options is what was done here in Washington. Joint and survivor option factors used for plans administered by Washington State have been simplified by eliminating the incremental ages of the members and collapsed from a single-year step differential to an overall plan average. The spouse/beneficiary age differential, however, is still in single year steps (see Table 7).

Table 7
Joint and Survivor 100% Payment Options
By Plan and Age Difference

Source: OSA

Spouse Age Difference		100% Joint and Survivor Option				
		LEOFF 2	PERS 1	PERS 2	TRS 1	TRS 2
Years older	2	0.798	0.849	0.813	0.897	0.869
	1	0.790	0.836	0.797	0.887	0.851
	0	0.780	0.822	0.779	0.877	0.832
Years younger	1	0.771	0.808	0.763	0.867	0.814
	2	0.760	0.796	0.748	0.857	0.797

Each Plan Different

There are different joint and survivor option factors for each plan that offers such a benefit: LEOFF 2, PERS 1, PERS 2, TRS 1 and TRS 2 (see Table 8). The factors differ because the demographic characteristics of members differ by plan as do the plan features. For instance, over 90 % of LEOFF 2 members are male while almost 3/4ths of TRS 2 members are female. The factors also differ because of plan features as well; the COLA provisions in the Plan 2 systems are more expensive than those in the Plan 1 systems thus making the reductions more pronounced as the member pays for the COLA for the survivor.

Table 8
Joint and Survivor Option Factors by Plan
No Age Difference Between Member and Beneficiary

Source: OSA

Retirement Plan	Joint and Survivor Option Factors		
	100.0%	66.7%	50.0%
LEOFF 2	0.780	0.842	0.877
PERS 1	0.822	0.874	0.902
PERS 2	0.779	0.841	0.876
TRS 1	0.877	0.914	0.934
TRS 2	0.832	0.881	0.908

Pop-Up

Should a designated survivor die before the plan member, there is now an adjustment of the retirement benefit called a "pop-up." This adjusts the benefit to where it would have been had no joint and survivor option been taken. Until 1997, once the joint and survivor option was chosen it was irrevocable; this despite the not uncommon instance of a designated survivor actually predeceasing the plan member.

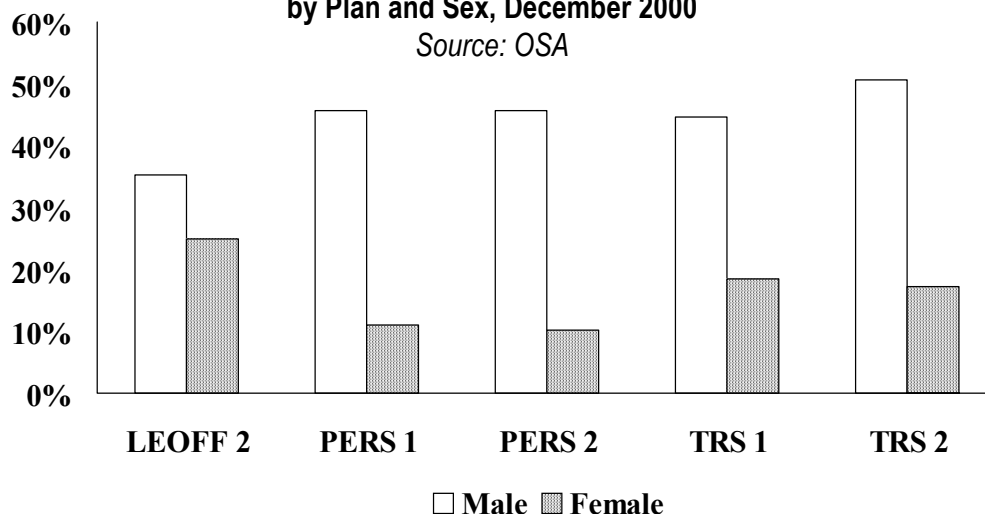
Who Uses

There are three factors that focus the likelihood of who will actually use the joint and survivor payment options. First, women, on average, live longer than men. Based on the most recent Life Expectancy tables used by the insurance industry, a woman born in 1997 could expect to live 78.8 years while a man born in 1997 could expect to live 71.8 years. That ubiquitous trend is born out by the experience of LEOFF, PERS, and TRS members (see Table 9). Second, men are, on average, older than their wives. Third, men are more likely to already have their own retirement benefit. As a result, the joint and survivor benefit is more likely to be used by men protecting the retirement income of their wives rather than by women protecting the retirement income of their husbands (see Graph 1).

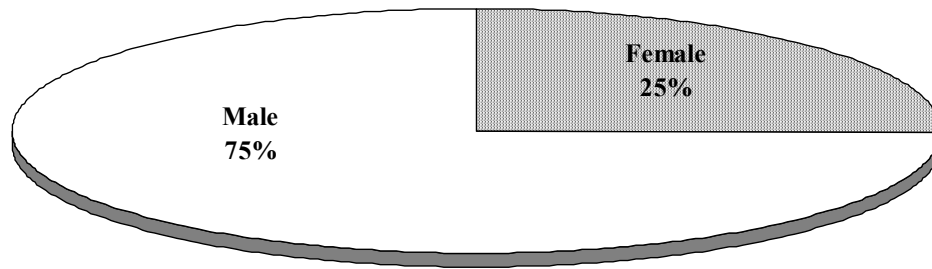
Table 9
Retirees, Average Age of Mortality, and Years of Retirement (YOR)
by Sex, Plan, and Disability: 1994 - 1999
Source: OSA

PLAN	Male			Female		
	#	Age	YOR	#	Age	YOR
LEOFF Service	251	73.8	18.3	9	80.0	20.7
LEOFF Disability	341	68.6	18.2	13	67.2	17.5
PERS Service	5,865	79.1	16.3	4,261	81.2	18.1
PERS Disability	432	67.2	12.1	318	67.1	11.7
TRS Service	1,441	77.6	16.8	2,950	85.6	22.7
TRS Disability	78	65.9	14.3	85	71.8	19.0

Graph 1
Retirees with a Joint and Survivor Option
by Plan and Sex, December 2000
Source: OSA



Graph 2
Retirees with a Joint and Survivor Option by Sex
Source: OSA



Of course there are women who use the joint and survivor options. Women who are significantly older than their spouse, or whose spouse has no retirement benefit, or who have a health history that signals some undue risk, may find a joint and survivor option reasonable. Other women may want to provide income protection for a non-spouse, disabled child, other relative, or even non-relative. But over-all, some three out of four of those taking a joint and survivor option are men (see Graph 2).

Survivor benefits and life insurance

The reductions in the retirement benefit that result from taking a joint and survivor option are akin to paying an insurance premium. They represent the cost of insuring the member so as to provide a survivor with a continuing benefit. The pop-up adjustment, should the designee happen to die prior to the plan member, is also akin to the member no longer needing that insurance and therefor no longer paying for it.

There are alternatives to taking one of the joint and survivor options. One, or a combination of the many forms of life insurance, personal savings, and deferred compensation are readily available choices. The common characteristic among these alternatives is the foresight necessary to implement them. To be an effective alternative to the joint and survivor options these programs must be started well before retirement.

Automatic, spousal eligibility-based survivor benefits

The LEOFF 1 and WSPRS joint and survivor benefit do not reduce the amount of the retiree's pension, making them distinct from other plans. If a spouse (or eligible child) meets the eligibility criteria, then they receive the survivor benefit. Each survivor benefit is paid for by the total contributions made by the state, employers, and employees to each retirement plan. Retirees from these plans do not have the option to select the amount of their continuing benefit nor to name a beneficiary other than their spouse.

The criteria for eligibility, and thus the number of survivors likely to arise in the plan, in combination with the size of the survivor benefit is a cost to the plan as a whole. This is in sharp contrast to the optional types of survivor benefits in the other plans - as each survivor benefit in those plans is paid for from the benefits of the individual that selects them, the number and characteristics of the survivor beneficiary population is largely irrelevant to overall plan costs.

Table 10
Profile of LEOFF Plan 1 Membership - 1998-2000

Year	Total	Active	Annuityants	Survivors	
				Number	% of Annuityants
1998	9,667	1,968	6,420	1,014	16%
1999	9,604	1,743	6,553	1,070	16%
2000	9,310	1,499	6,684	1,096	16%

It is difficult to accurately determine how many survivors that will exist for each of the two plans with automatic, spousal eligibility-based survivor benefits. The criteria in each of LEOFF plan 1 and WSPRS are very different. LEOFF plan 1 is already closed to new membership, however, and as the State Patrol benefits with the automatic survivor benefit will close to new members after January 1, 2003.

Qualified spouses of LEOFF plan 1 retirees are limited to those lawfully married to the member for one year prior to retirement or separation from service. If the member dies with qualifying children, then this may increase the amount of the survivor benefit payable to the surviving spouse, or the children may qualify for an independent survivor benefit if the member has no spouse.

The LEOFF plan 1 survivor benefit is relatively large - the greater of 50% of the member's final average salary if active at the time of death, the amount of retirement allowance the vested member would have received at age 50, or the full continuation of the member's benefit if the member is retired or on disability. The full continuation benefit, a common result for survivors, includes a cost-of-living increase equal to the consumer price index each year.

Table 11
Profile of WSPRS Membership - 1998-2000

Year	Total	Active	Annuityants	Survivors	
				Number	% of Annuityants
1998	1,738	929	582	98	17%
1999	1,722	968	604	110	18%
2000	1,740	1,013	631	104	16%

The Washington State Patrol Retirement System makes post-retirement spouses who have been married to the member for two years prior to the member's death eligible for the survivor benefit. The survivor benefit is the lesser of 50% of average final salary or the retirement allowance paid to the member. The survivor's benefit includes a COLA of up to three percent per year. The cost of the survivor benefits in the automatic systems is linked to both the size of the benefits, and the number of survivors that are eligible at the members' deaths.

Tables 10 and 11 do not reflect one very important difference between the LEOFF plan 1 and WSPRS: LEOFF plan 1 is a closed plan which has accepted no new members since 1977, and WSPRS is still accepting new members as of the date of this report. This can significantly affect the percentages of survivors verses annuityants. Another comparison, how many members die leaving an eligible survivor is in some ways a more useful comparison of the effect of each plans eligibility criteria.

Table 12
LEOFF Plan 1 Member Active and Retired Deaths - 1998-2000

Year	Active Deaths	Retired Deaths	Total Deaths	Died, No Survivor	
				Number	% of Total Deaths
1998	13	101	114	62	54%
1999	9	131	140	74	53%
2000	4	164	168	95	57%
Total	26	395	422	231	55%

Table 12 demonstrates that over the past three years 55% of LEOFF plan 1 members died without an eligible survivor. The eligibility rules in LEOFF plan 1, in particular the requirement that the spouse be married to the member prior to separation from service, are likely a factor in the difference between the number of members who have eligible spouses. Table 13 provides a comparison to WSPRS, which has eligibility rules including spouses that may have been married to members after retirement or disability-related separation from service.

Table 13
WSPRS Active and Retired Deaths and Survivors - 1998-1999

Year	Active Deaths	Retired Deaths	Total Deaths	Died, No Survivor	
				Number	% of total deaths
1998	0	4	4	1	25%
1999	1	14	15	1	7%
2000	0	12	12	9	75%
Total	1	30	31	11	35%

While the data for the much smaller WSPRS is limited, the large difference in the percentage of members who died without leaving a survivor suggests that the difference in the eligibility rules substantially impact the number of resulting survivors.

Another factor that may affect the difference in the rate members leave survivors is the rate that LEOFF plan 1 members have left membership because of disability before reaching the retirement age of 50. One year before separation from service is the date determining if a spouse is eligible for the LEOFF plan 1 survivor benefit.

The average age of retirement for LEOFF plan 1 members was 53 years. According to the Washington Health Care Authority's study on the age of men when they marry, approximately 9.5 % of men marry at or after the age of 50. Of a total of 41,443 Washington marriages in 1998, 3,953 involved men over the age of 50. These numbers nearly double when examining the number of men who marry after age 45.

Table 14
Marriages by Man's Age in Washington State - 1998

	<20	20-24	25-29	30-34	35-39	40-44	45-49	50-54	55-59	60-64	65+	Total
#	1,267	9,252	9,943	6,489	4,732	3,351	2,344	1,594	914	532	913	41,443
%	3%	22%	24%	16%	11%	8%	6%	4%	2%	1%	2%	100%

Table 15
LEOFF Plan 1 Retirements and Disabilities by Age - 1994-1999

Age	Service Retirement	Disability Retirement	Total
<34	-	6	6
35-39	-	62	62
40-44	-	221	221
45-49	-	417	417
50-54	353	308	661
55-59	123	73	196
60+	53	14	67
Total	529	1,101	1,630

Table 15 demonstrates this during the 1994-1999 period, where 706 of the total 1,630 separations from service, 43.3%, were by disability retirement prior to age 50. This is important because spouses who marry members less than one year before the disability retirement are also ineligible for the LEOFF plan 1 survivor benefit. An exception to the one year requirement exists for members who die in the line of duty.

Analytic Approach

The purpose of this report is to define the issues that would be raised by providing additional flexibility to retirees regarding their choice of a survivor option or their selection of a beneficiary, both after retirement and before retirement at divorce. Options for types of benefit flexibility that might be provided are included in this report and the report will identify areas where the issues and analysis may differ depending on whether the member is a retiree from LEOFF Plan 1 and the State Patrol Retirement System or a retiree from PERS, TRS, LEOFF Plan 2.

Significance of the Issue to Policy

Increased Flexibility

The fundamental purpose of any retirement system is to allow a member to prepare for their financial needs following their retirement from employment. The JCPP has previously stated that retirees should have more flexibility in determining the form and timing of their benefits. Currently, a retiree is required to make their best estimate of their future needs regarding a survivor benefit at the time they retire. Unanticipated events following retirement such as divorce, marriage, or the death of a spouse may significantly alter a retiree's needs.

A benefit that provides the retiree with some flexibility to adapt to changing circumstances will reduce the necessity for the retiree to guess what their future needs will be and lessen the financial impacts on the retiree if they guess wrong. Inflexible application of retirement benefits in Washington has at times placed retirees in distressing circumstances.

Protection of Spouse and Community Property

The policy issues involved in providing more flexibility in survivor benefits to spouses are often very different from the policies involved in providing survivor benefits to non-spouses or children. The protection of spouses is a State policy which extends beyond the scope of pensions to many other areas of law such as community property.

Community property law raises important considerations for flexibility in survivor benefits. During a marriage property may be owned by one spouse individually, or by both in a fashion similar to a partnership in which case it is called community property. The central provisions of community property law are contained in chapter 26.09 RCW, but the principles are pervasive in Washington law.

Generally, property acquired by a husband or wife during their marriage, including wages and benefits, is community property owned by both. If a retiree is married, spousal consent is required to decline a survivor benefit at retirement or designate anyone but the spouse as the beneficiary.

A survivor beneficiary may be designated prior to a member's retirement if DRS is served with a marriage dissolution order that requires the department to designate an ex-spouse as a survivor beneficiary entitled to a particular survivor option. A dissolution order may also require that DRS divide any periodic retirement payments or lump sum withdrawals between a member and their ex-spouse.

The Table 16 illustrates the scope of divorce among retired groups:

Table 16
**Divorces and Annulments Among
Washington Retirement-Aged Women
1995 and 1997**

Year	Age			
	50-54	55-59	60-64	65+
1995	1,124	532	264	303
1997	1,415	643	279	314

Washington State Vital Statistics, 1995, 1997.

Providing more flexibility to retirees regarding a survivor benefit may encourage the use of the survivor benefit to protect spouses. Conversely, rigid rules regarding survivor benefits may discourage their use.

Revisiting survivor benefits after divorce or at post-retirement divorce

Among the most common issues raised by the survivor benefits in the state retirement systems involve divorced spouses. Current law does not allow a ex-spouse designated as a survivor to have the designation removed at divorce. Occasionally this results in frustration for the member at or after divorce.

One circumstance is illustrated by a member and spouse who agree on a property settlement at divorce which awards the member all of their state retirement system benefit. The member may have even foregone other assets or support in the negotiation of their property settlement agreement to obtain the entirety of their retirement benefit. Some time later, the member wishes to either have the actuarial reduction from their benefit removed or designate a new spouse as their survivor. State law does not permit their property settlement agreement to take the survivor benefit away from their ex-spouse, so this part of their agreement has no effect.

One solution could involve the re-opening of the property settlement agreement. Such a re-opening could allow the members to split their benefits and assets differently (including the value of the survivor benefit), correct a misunderstanding by one or both parties during their divorce, or take advantage of a new form of benefit that might be created by the Legislature.

- *The property settlement agreement - court order and contract*

The agreement to divide property between divorcing spouses can be in part both an decree by the trial court and, depending on the circumstances, frequently a contract between the spouses. While divorce agreements are commonly modified in areas relating to the custody and support of children, and may be modified with respect to spousal support obligations, significant barriers exist to modification of property distribution agreements incorporated into dissolution decrees.

Dissolution decrees arise under Chapter 26.09 RCW. The court may examine the total of the property possessed by the divorcing parties and make an equitable division considering factors such as the extent of community and separate property, the duration of the marriage, and the economic circumstances of the divorcing spouses. Contrary to common understanding, the court is not limited to distributing community property, rather the court may generally distribute all property between the spouses in an equitable manner. The court's power to fully divide property in a "just and equitable" fashion may be limited, however, if the parties choose to enter into a property settlement agreement.

The divorcing spouses may enter into a property settlement agreement at some time prior to their divorce. These contracts are provided for in RCW 26.09.070, and may serve several purposes. Prominently, the terms of such an agreement is binding upon the court as the division of property between the spouses unless the court finds the contract unfair at the time of its execution¹. When the trial court grants the dissolution decree, the property settlement agreement may be incorporated into the decree.²

RCW 26.09.070(3) If either or both of the parties to a separation contract shall. . . petition the court for dissolution. . . , the contract. . . shall be binding upon the court unless it finds, after considering the economic circumstances of the parties and any other relevant evidence produced by the parties on their own motion or on request of the court, that the separation contract was unfair at the time of its execution.

¹See, e.g. Washington Judge's Family Law Benchbook, Superior Court Judges' Education Committee, Office of the Administrator for the Courts, Second Edition, 1996.

²See, for example, Shaffer v. Shaffer, 47 Wash. App. 189, 733 P.2d 1013 (1987).

Subsection three of RCW 26.09.070 restricts the authority of the courts to modify the contents of the property settlement agreement to a single circumstance: where the agreement was unfair when it was executed.³

- *Statutory and Court Rule basis for re-opening*

The re-opening of property distribution orders is generally disfavored by statutory law and the courts, but in very limited circumstances does occur. Consistently, the courts have noted that there is a strong public policy interest in favor of the finality of dissolution decrees.⁴

State law provides for the re-opening of property division orders:

RCW 26.09.170. Modification of decree for maintenance or support, property disposition – Termination of maintenance obligation and child support – Grounds

(1) Except as otherwise provided in subsection (7) or RCW 26.09.070, the provisions of any decree respecting maintenance or support may be modified: (a) Only as to installments accruing subsequent to the petition for modification or motion for adjustment except motions to compel court-ordered adjustments, which shall be effective as of the first date specified in the decree for implementing the adjustment; and, (b) except as otherwise provided... only upon a showing of a substantial change of circumstances. The provisions as to property distribution may not be revoked or modified, unless the court finds the existence of conditions that justify the reopening of a judgement under the laws of this state. [emphasis added]

Separate language is included in the statute clarifying that the standard for modifying the property distribution is different than for maintenance or support - and it is a more stringent standard.

Prior to 1973 state law was even more preclusive against re-opening property divisions, stating specifically that the court's division was "final and conclusive."⁵ This is the rule that the courts have generally continued to enforce, with two narrow exceptions: if the property division is disguised spousal maintenance,⁶ or if grounds for modification exist on Court Rule (CR) 60(b) grounds.⁷

CR 60(b) generally permits relief from a final judgment in extraordinary circumstances on a showing of manifest injustice⁸. In the case of modification of a property distribution, a court must find a manifestly unjust result of the judgement that justifies reopening under RCW 26.09.170.⁹

³Shaefer, 47 Wash. App. at 194.

⁴See, e.g. In re the Marriage of Knies, 2001 Wn. App. Lexis 405, *6.

⁵RCW 26.08.110, prior to 1973.

⁶See, e.g. In re Marriage of Coyle, 61 Wn. App. 653, review denied, 117 Wn.2d 1017(1991).

⁷See Washington Family Law Deskbook, Wash. St. Bar Assoc. 2d ed. 2000 at 32-25 through 32-29.

⁸ In the Matter of the Marriage of Burkey, 36 Wn. App. 487, 490(1982).

⁹In re Marriage of Larkin, 2001 Wn. App. Lexis 405, (March 8, 2001).

Extraordinary circumstances and manifest injustice presents a high standard for re-opening under CR 60(b). A recent line of Washington appeals court cases beginning in 1982 with *In the Matter of the Marriage of Lavonne Burkey*, 36 Wn. App. 487 (1982), illustrate the where Court Rule 60(b) was, or was not sufficient to re-open a dissolution decree. Erroneous legal advice given to one party was not enough to re-open a dissolution decree and the property division it contained¹⁰. Nondisclosure by one spouse of the value of an known asset to the other was not sufficient to re-open the final decree.¹¹

Decrees were re-opened and modified where the dissolution stated that the non-member spouse would receive half of the member's retirement benefit, and the member drew disability benefits after the entry of the decree rather than retirement benefits and claimed that this discharged them of obligation to pay under the decree.¹²

A change in federal law regarding the divisibility of military retirement benefits was found to be a sufficiently extraordinary circumstance to allow final decrees to be reexamined through a CR 60(b) motion¹³. The court emphasized the "limited nature of this exception" to the doctrine of the finality of judgements,¹⁴ including that the period during which the federal rules that prevented the military retirement benefits from being divided were in effect for only 20 months, so the members never had a "settled expectation" that the retirement benefits could not be divided.¹⁵

- *Issues in re-opening property distribution agreements*

- The courts' aversion to address what should have been decided in a prior action

Occasionally constituent inquiries raise the issue of a failure to either account for the value of the survivor benefits in a property settlement agreement, or for having made an incorrect assumption that the survivor benefit can be returned to the member upon divorce. These scenarios raise the issue of whether the court should re-open the property distribution agreement and re-allocate the property, either under current law or in the event that a new benefit option is made available.

¹⁰Burkey, 36 Wn. App. 487.

¹¹In the Matter of the Marriage of Maddix, 41 Wn. App. 248, 253 (1985).

¹²Knies, 96 Wn. App. 243.

¹³In the Matter of the Marriage of Flannagan, 42 Wn. App. 214, review denied, 105 Wn.2d 1005 (1986).

¹⁴Id. at 222.

¹⁵Id. at 223.

In the first of these scenarios, where the value of the survivor benefit may have in some way not been properly accounted for in the divorce, a number of different legal issues are raised. One important one involves a concept called “res judicata,” which is essentially what courts call their prohibition on parties re-trying claims that were part of, or should have been part of, an earlier proceeding.¹⁶

Generally, “res judicata” provides that a party that fails to exercise reasonable diligence at the time of their original court proceeding and include a particular claim should be barred from returning to court and raise the same issue between the two parties a second time.

A related issue to the court’s reluctance to address what should have been decided in a prior action is where one of the parties in some way misunderstood what they were dividing, and want action to correct the mistake.

- Revisiting a mistaken division

Sometimes a mistake is made in the property division agreement between the divorcing spouses. The non-revocability of the survivor benefit may not be understood by one or both parties. For example, the member may receive “all pension benefits” in their divorce, while this is in fact not possible under current law. The failure of the parties to properly value the survivor benefit in a property distribution agreement has occasionally been raised as well.

The court’s place upon the parties the duty to determine the nature and value of assets presented to the court for division¹⁷. It is generally incumbent upon the divorcing parties to determine the actual value of the assets that they are dividing. If one of the parties chooses not to make an adequate examination, courts have stated that they should not be allowed to return to court to do what should have been done prior to the entry of the original decree.¹⁸

- *Discussion*

- Permitting willing parties to return to court

Could former spouses whose divorce left the non-member spouse a survivor benefit agree in some fashion to return the survivor benefit to the member, or convert it to some other benefit? In ideal circumstances a proposal might be created to allow this, though extensive safeguards might be needed to ensure that both parties were indeed willing, and that the expenses for new proceedings be equitably distributed.

¹⁶See Hansen v. Hansen, 87 Wash. App. 320, 941 P.2d 1108 (1997) for a discussion of res judicata in the context of re-opening of property distribution agreements. Hansen notes that in Washington res judicata has been used by the court to refer to the related concepts of “issue preclusion” and “claim preclusion.”

¹⁷Maddix, 41 Wash. App. at 253.

¹⁸Id.

The two principle methods by which the non-member spouse received the survivor benefit (PERS, TRS, LEOFF plan 2, etc.) are by the choice of the member and spouse at retirement, or by the court's instruction that the member choose the former spouse as their survivor at retirement. In each case, different considerations of whether the parties should be able to revisit the survivor benefit seem to apply.

A member and spouse that chose the survivor benefit at retirement, and then later divorced and were unable to remove the survivor benefit, were never able to make a choice about the disposition of the survivor benefit in a divorce proceeding. In contrast, divorcing spouses that had the survivor benefit "pre-chosen" in their pre-retirement divorce effectively already had an opportunity to choose to allocate the survivor benefit to the non-member spouse when the member retired.

- Allowing an unwilling party to be forced to return to court

If the non-member former spouse does not want to revisit the division of their pension benefits, should the member be able to compel them to return to court? While there are possibly legal issues that are discussed below, many policy questions are also raised.

As the changing of a court-ordered division of retirement benefits would presumably involve similar court proceedings to those that divided the benefits initially, an unwilling party might be forced to incur substantial additional costs to appear and secure legal representation. Who should bear those costs?

Should it be possible for a subsequent proceeding to reduce either party's share of the retirement benefit, or only do so if they receive reasonable compensation in return? The member and former spouse presumably had their property divided in an equitable manner when their divorce decree was entered, there may be an interest in the preservation of the equity found in the original distribution.

- Legislative retroactive modification of divorce decrees

A property settlement agreement may be incorporated into a court decree. The agreement may be an actual contract between the two parties depending on how the divorce came about, and as a contract presents additional issues to subsequent legislative change beyond the obstacles to altering the power of the courts to revisit the property settlement portion of divorce decrees.

Legislative voiding or retroactive modification of a contract between private parties raises the constitutional issue of the impairment of contracts. The Washington State Constitution, article 1, section 23, provides: "No bill of attainder, ex post facto law, or law impairing the obligations of contracts shall ever be passed." This prohibition applies to any form of legislative action, but different standards of impairment apply to public and private contracts.¹⁹

¹⁹ Washington Fed'n of State Employees v. State, 127 Wn.2d 544, 560 (1995).

The prohibition on impairment of contracts is not literal or absolute however, and courts apply a different test for public(with the state) and private contracts²⁰. The U.S. Supreme Court articulated a three step method for analyzing impairment of private contract claims in 1983. First, a statute would be examined for “operating as a substantial impairment of a contractual relationship”; second, if a substantial impairment was found the statute must serve “a significant and legitimate public purpose”; and if the first two steps are satisfied, thirdly that the “legislation is based upon reasonable conditions... and is appropriate to the public purpose justifying... adoption.”²¹

The rights that retirees have to their promised benefits, for example, are in the nature of contract rights established by statute. Their protection through the Bakenhus²² line of court cases is an important example of the restrictions on the impairment of public contracts in the pension area.

The less stringent test on impairment applies to private contracts. The private contract involved in this analysis is between the divorced member and spouse often made to divide their property, and then submitted to the court for inclusion in their marriage dissolution order. If a change in statute affecting vested contractual rights between private parties is intended to be retroactive, and is neither curative nor remedial, there may be an issue of violation of constitutional rights.²³

It is worth noting however that contract rights are a form of property, and as such in many cases may be impaired or taken for a public purpose provided that just compensation is paid to the owner.²⁴

Legislative action that retroactively voids court decisions also presents due process issues, apart from any substantive rights. A statute may not operate retroactively to deprive a person of property without due process of law²⁵. A statutory change that effectively eliminated the survivor benefit awarded to the ex-spouses of members in a past divorces without at least initiating a new legal proceeding might create problems related to individual's right to due process.

- *Anti-Selection*

Providing survivor benefit flexibility after retirement raises significant actuarial issues in terms of the funding of retirement benefits. This is primarily so because of the fact that life expectancy, both of the retiree and their designated beneficiary, is a critical factor in the computation of the cost of the survivor benefit.

²⁰Id. at 561.

²¹Energy Reserves Group, Inc. v. Kansas Power and Light Co., 459 U.S. 400, 411 (1983).

²²See Bakenhus v. Seattle, 48 Wn. 2d 695 (1956) and following decisions.

²³In the Matter of F.D. Processing, Inc., 119 Wn.2d 452, 460 (1992).

²⁴United State Trust Co. v. New Jersey, 431 U.S. 1, 19 (1977).

²⁵Graves v. Dunlap, 87 Wn. 648 (1915).

“Anti-selection” is an actuarial term which refers to a person making a choice against actuarial predictions because of some knowledge regarding their life expectancy. A classic example of anti-selection would be a retiree who chooses a survivor benefit because they learn they are suffering from a terminal illness. Anti-selection can only take place when the member can make a choice.

To avoid anti-selection we have inflexible systems which do not allow for choices after retirement. This inflexibility also reduces the usefulness of the retirement systems. There is always a tension or tradeoff between the flexibility or usefulness of a retirement system and the cost of anti-selection but the risk of anti-selection can be managed by placing some restrictions, such as a waiting period, on the exercise of options.

Anti-selection concerns have resulted in specific waiting periods, or “windows”, in recent additions to the optional survivor benefit plans. The 2000 legislature created a post-retirement marriage option in PERS, SERS, TRS, and LEOFF plan 2. Following the implementation period, an eligible member could choose a survivor benefit for a post-retirement spouse, but only during a one year “window” that opens one year after their post-retirement marriage.

- *Cost to the Trust Fund*

The survivor options available to a member at retirement are calculated to be actuarially equivalent to an unreduced benefit and to each other. Switching between these options at a later date may not result in a cost to the trust fund. The primary cost risk is the danger of anti-selection as described above. If the risks of anti-selection were managed through restrictions on the exercise of some options, then the result might be no cost or a negligible cost to the retirement fund.

- *Beneficiary Selection*

A survivor benefit is automatically provided at retirement for the spouses of LEOFF Plan 1 and WSPRS retirees. These retirees do not have the option to provide a survivor benefit to anyone other than their spouse, such as their children or ex-spouse. Retirees from PERS, TRS, LEOFF Plan 2 and JRS have the option to designate non-spouses as their beneficiary. However, tax implications may be raised if the designated beneficiary is a non-spouse who is more than ten years younger than the retiree.

Legislative History

In 1985, the legislature granted authority to the Department of Retirement Systems (DRS) to adopt actuarially equivalent retirement options. The “pop up” benefit which was implemented in 1996 was adopted pursuant to this authority. Other actuarially equivalent options which would provide some additional flexibility to survivor benefits might be adopted pursuant to this same authority (see Appendix, item B).

Senate Bill 5742 was introduced during the 1997 session to address the issue of allowing a court to cancel the survivor benefit to an ex-spouse if the ex-spouse violated the terms of a restraining order which had been filed against them. The bill did not pass.

House Bill 2666 was introduced during the 1998 session to address the issue of the automatic cancellation of the survivor benefit for spouses of LEOFF Plan 1 retirees when there is a post-retirement divorce. This same issue applies to spouse of State Patrol retirees. The only current exception to the automatic cancellation is in the case of a LEOFF 1 ex-spouse who was married for thirty years, including twenty years before retirement, and who was awarded the survivor benefit by the court in a divorce decree. The bill did not pass.

Senate Bill 5727 was introduced in the 1999 session to qualify spouses who were married to LEOFF Plan 1 members for less than 1 year prior to retirement for the plan's non-actuarially reduced full survivor benefit. The proposed benefit would include subsequent, post-retirement marriage spouses, even if the member was married to an earlier spouse who predeceased them (and was an eligible survivor beneficiary) after the member retired. The bill did not pass. Similar legislation, HB 1432, was introduced in the 2000 session with the qualification that the survivor must have been married to the member for five years prior to death, and must be age 55 before benefits begin.

House Bill 2604 was introduced in the 2000 session by recommendation of the Joint Committee on Pension policy. It was adopted, and its provisions become effective as rules are adopted in 2001 and 2002. It added two new survivor benefit flexibility options, first allowing a spouse in a post-retirement marriage to be made a survivor beneficiary during a one year window, and second allowing a non-spousal survivor designation made by a member at retirement to be revoked, removing the actuarial reduction to the member's benefit.

Several bills relating to survivor benefits in LEOFF plan 1 were introduced into the 2001 session, including two recommended by the JCPP(HB 1050 and HB 1215). None were adopted.

Other Relevant Information

The Office of the Attorney General wrote a legal opinion in 1977 (AGLO 1977 No. 41) which stated that in the event a member of the public employees retirement system, upon retirement, selects a particular form of retirement allowance, the member may not thereafter (during his or her retirement) revoke the selection made at the time of retirement and either choose a different retirement allowance or change a beneficiary designation.

The 1985 legislation which authorized DRS to adopt actuarially equivalent retirement options would arguably supercede this 1977 opinion and allow DRS to adopt actuarially equivalent post-retirement options for choosing a different retirement allowance or changing a beneficiary designation without further legislative action. However, new legislation would serve several purposes:

- DRS is not required to adopt new options pursuant to their 1985 grant of authority and might be reluctant to develop new options if they feel that their authority to adopt new options needs clarification;
- New legislation would allow the Legislature to provide some direction to DRS regarding the form any new retirement options would take; and,
- The legislative process would allow for input from retirement system members and retirees as to what types of options they would like.

The creation of new retirement options may result in the need for new actuarial factors which would be developed by the Office of the State Actuary.

Possible Approaches

One or more approaches could be developed to increase survivor option flexibility for members.

- Optional, actuarially reduced survivor benefit for ineligible spouses.

An optional, actuarially reduced survivor benefit could be added to LEOFF plan 1 for post-retirement spouses. Within a one-year window opening one year from the date of the post-retirement marriage, the member could take an actuarial reduction to their benefit and designate their new spouse as their survivor beneficiary. The optional survivor benefit would be limited to retirees whose benefits are not subject to a property settlement under a court decree of separation.

The actuarial reductions under such an approach would be approximately as shown on Table 17.

Table 17
Actuarial reductions for a LEOFF plan 1 optional survivor benefit.

Difference in Age of Survivor and Member	Actuarial reduction, Joint & 100% Survivor Benefit
5 years older than member	0.82
No difference in age	0.77
5 years younger than member	0.73
10 years younger than member	0.69
15 years younger than member	0.65

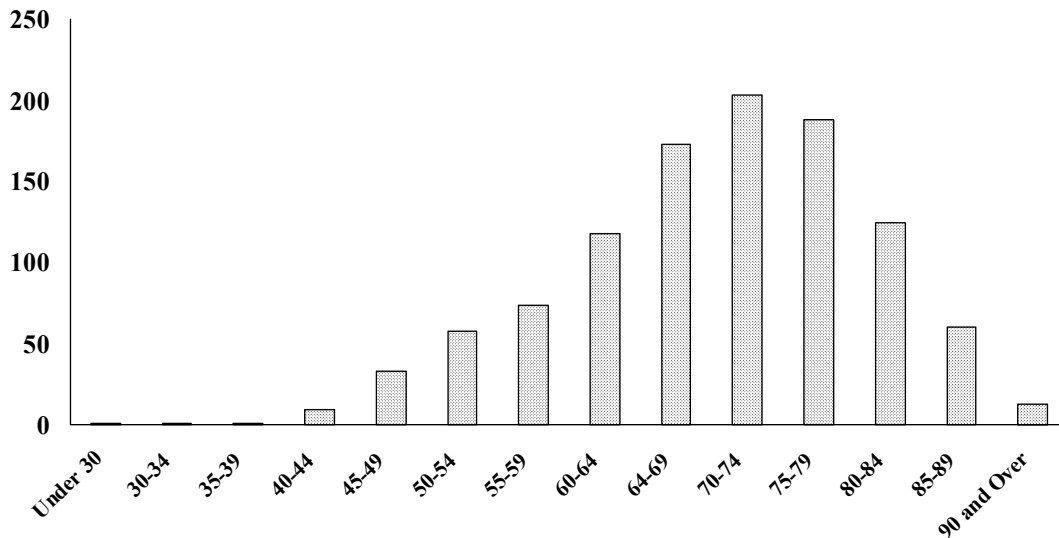
- *Remove the eligibility requirements for spousal survivors*

The requirement that a spouse be married to a member for one year prior to separation from service could be removed. This would add additional beneficiaries and costs to the system by providing a full continuation of members' benefits to individuals who would not receive LEOFF plan 1 benefits under current law.

During the 1999 legislative session, Senate Bill 5727 proposed removal of the spousal survivor eligibility requirements. The 1999 proposal would have also continued eligibility for the survivor benefit to ex-spouses of retirees who were awarded survivor benefits in a court order pursuant to the divorce.

During the 2000 legislative session, House Bill 1432 proposed changing the survivor eligibility requirements to include any spouse who was married to the member for five years at the time of death to begin collecting the current LEOFF plan 1 survivor benefit at age 55. An analysis of the age of the LEOFF plan 1 survivors for 1999 was prepared in 2000. It suggests that about 10 percent of surviving spouses might not be initially eligible because of their age. No data is available on the length of members' marriage to their spouses at time of death.

Graph 3
Age of LEOFF Plan 1 Spousal Survivors - 1999



It is difficult to accurately assess how many members of LEOFF Plan 1 have survivors if the spousal eligibility requirements are removed or modified. If all LEOFF Plan 1 members left a surviving spouse the actuarial impact of removing the one-year prior to separation from service requirement would be an approximate \$450 million increase in the Present Value of Fully Projected Benefits. The actual amount would be less, depending on any criteria established, as not all members would die with a spouse.

- *Create options for dividing benefits into separate, single-life benefits*

Upon divorce, a member and divorcing spouse could be permitted to divide their benefits into two separate single-life benefits. Separate single-life benefits are essentially two benefits payable over the life of each of the spouses almost as if they are separate members. The separate single-life benefit structure fits within the structure of the optional, actuarial reduction survivor benefits, but does not fit as easily within the automatic, eligibility-based plans like LEOFF plan 1.

In a post-retirement divorce situation, the separate single-life benefits should only be available in cases where the non-member spouse was selected as a survivor beneficiary at retirement to avoid anti-selection problems.

The separate single-life benefit option offers several advantages over current provisions. The benefits to the member and ex-spouse are not dependent on each other. For example, a non member ex-spouse who has only a survivor benefit that could not be removed at divorce receives no benefits until their former spouse dies, keeping their lives in a sense linked to one another.

In a post retirement divorce situation the separate single-life benefit option also permits the value of any existing survivor benefit to be removed, and the total benefit to be divided between the divorcing spouses by the court. A non member ex-spouse could also receive a superior benefit to the current option of a portion of the member's benefit payments - unlike the portional benefit, the separate single-life benefit does not cease upon the member's death.

A separate single-life benefit option also addresses the issue of survivor benefit protection for subsequent spouses in two ways. First, the survivor benefit does not need to be pre-assigned to a first divorcing spouse in order for that spouse to have a lifetime benefit. Second, after division into single-life benefits, the member may select a subsequent spouse at either retirement or post retirement marriage for survivor benefit coverage. The actuarial reductions made to create a survivor benefit after division into separate would be made solely to the member's single-life benefit.

Executive Committee Recommendation

Different options for dividing benefits at divorce can be provided for all retirement plans, however different approaches need to be taken in the "optional" plans and the "automatic" plans. The approaches of this proposal for each are detailed below.

Approach in "optional" plans:

Most of the retirement plans are in this category, including PERS, TRS, SERS, LEOFF plan 2, and the future State Patrol plan. In each case the department shall adopt rules by July 1, 2003 to make a new option available at divorce - a division of the total benefits of the member and divorcing spouse into two separate single-life benefits payable for the life of that individual.

If the division occurs before the member retires, a member who later remarries will remain subject to the spousal survivor benefit requirements when they retire. Any subsequent reductions of the member's benefit shall be made solely to the member's separate benefit. The divorced spouse of the member will be eligible to begin their single life benefit upon reaching the normal retirement age in the plan of their divorced spouse - age 60 in the plans 1 and age 65 in the plans 2.

If the division occurs after the member has retired, the separate single-life benefit option will only be available if the non-member spouse was selected as a survivor at retirement. This restriction is designed to limit anti-selection. The non-member spouse will be eligible to begin collecting their single-life benefit immediately, and in the event that the member remarries they will have the option of taking a reduction to their single life benefit and select a survivor benefit for their post-retirement marriage spouse.

Separate single-life benefits are exempt from minimum benefit provisions, each may receive annual increases accounted for in the actuarial division of the benefit, and in the case of plan 3 only the member is eligible for gain-sharing payments subsequent to division into single-life benefits.

Approach in "automatic" plans:

There are only two plans in the "automatic" category, LEOFF plan 1 and the current State Patrol plan. In each of these plans a new option for division of benefits at divorce would be added, permitting a divorcing spouse to receive both a portion of the member's benefit, and a portion of any eligible surviving spouse's benefit that might be created in the future. This is somewhat similar to the approach in the 2001 legislation SB 5142, but would divide the existing spousal benefit, rather than create an additional benefit for the life of the divorcing spouse.

In LEOFF plan 1 there is no survivor benefit available for spouses who marry members who have already separated from service. The proposal incorporates the approach of SB 5144, adding an optional, actuarially-reduced spousal survivor benefit during a window opening one year after a post-retirement marriage.

FISCAL NOTE

REQUEST NO.

RESPONDING AGENCY:	CODE:	DATE:	BILL NUMBER:
Office of the State Actuary	035	12/04/01	Survivor Benefits

SUMMARY:

This bill impacts the Law Enforcement Officers' and Fire Fighters' (LEOFF), Teachers (TRS), School Employees (SERS), Public Employees' (PERS), and Washington State Patrol (WSP) Retirement Systems by instructing the department to implement by rule new options for the division of benefits at divorce.

In those plans featuring an optional, actuarial reduction-type of survivor benefit, a benefit may be divided between the spouse into actuarially-equivalent single life benefits at divorce. In those plans featuring an automatic-type of survivor benefit, LEOFF Plan 1 and WSP Retirement Systems current plan, a non-member ex spouse may receive both a portion of the member's benefit upon divorce. A supplemental actuarial reduction-type of survivor benefit is also added for post-retirement marriages in LEOFF Plan 1.

Effective Date: 90 days after session.

BACKGROUND DISCUSSION:

State retirement plans feature two principle types of survivor benefit. The most common are the optional, actuarial reduction-types that are irrevocably chosen at retirement, or occasionally upon pre-retirement divorce. LEOFF Plan 1 and WSP Retirement System feature automatic types that only qualifying surviving spouses receive.

MEMBERS IMPACTED:

Members of the LEOFF, TRS, SERS, PERS and WSP Retirement System who divorce after the adoption of the rules will have the new options available to them.

FISCAL IMPACT:

None.

Technical/Other Corrections

Background:

Technical issues and statutory correction matters were brought before the Joint Committee on Pension Policy during the 2001 interim. The issues were grouped into three bill proposals.

Committee Activity:

Presentation:

December 10, 2001, Full Committee Meeting

Proposal Approved:

December 10, 2001, Full Committee Meeting

Recommendation to Legislature:

Three bills are recommended to the legislature. The first corrects issues related to 2001 legislation SB 5937 and SB 6167, many of which are related to the non-passage of SB 6166, the LEOFF 1 termination bill. The second resolves several issues on conforming with federal law on veterans in PERS plan 1 and WSPRS. The third addresses the issue of the transfer of career seasonal employees and military leaves of absence from PERS 2 to PERS 3.

Staff Contact:

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Technical/Other Corrections

A. Technical Corrections:

Section 1: Corrects a section amended by SB 5937 which contained erroneous cross references prior to amendment last year. The referenced sections were intended to address issues relating to teacher participation in continuing contracts. RCW 28A.405.900.

Section 2: Removes references to the "restated LEOFF" that would have been created by the proposed termination of LEOFF plan 1. Two versions of the statute resulting from separate bills enacted during 2001 are reconciled. RCW 41.45.060.

Section 3: Removes references to the "restated LEOFF" and restores funding language removed from the section as part of the same LEOFF plan 1 termination bill. RCW 41.45.010.

Section 4: Removes references to the "restated LEOFF" and restores funding language removed from the section as part of the same LEOFF plan 1 termination bill. RCW 41.45.020.

Section 5: Removes references to the "restated LEOFF" and restores funding language removed from the section as part of the same LEOFF plan 1 termination bill. RCW 41.45.050.

Section 6: Corrects a mistaken SERS cross reference. RCW 41.35.700.

Section 7: Corrects a mistaken SERS cross reference. RCW 41.35.510.

Section 8: Adds references to TRS and PERS plan 3 to Department of Retirement System provisions on benefit division orders. RCW 41.50.790.

Section 9: Repeals one version of RCW 41.40.037 that would have come into effect in 2004. Made redundant by the Governor's veto of the sunset provisions in the retire/rehire bill of 2001, SB 5937. RCW 41.40.037.

B. Conformance to Federal Requirements on Veterans:

Section 1: The definition of the Vietnam Era used for PERS plan 1 and WSPRS is changed to include veterans who served in the Republic of Vietnam between February 28, 1961 and May 7, 1975. RCW 41.04.005.

Section 2: The prohibition on military service credit in PERS for members receiving full military retirement is removed. RCW 41.40.170.

Section 3: The prohibition on military service credit in WSPRS for members receiving full military retirement is removed. RCW 43.43.260.

C. Seasonal and Military Leave Employees Transfer to PERS 3:

The single new section of the bill allows seasonal career employees the opportunity to transfer to PERS plan 3 and receive the additional transfer payment providing they earn service credit between March 1, 2002 and March 1, 2003, regardless of their employer's transfer window. A seasonal career employee is one employed by an employer on a seasonal basis for four consecutive seasons.

Members on military leave of absence during their employer's transfer window will have the opportunity to transfer to plan 3 and receive the additional transfer payment providing they purchase service for required periods within six months of their return from military leave.

FISCAL NOTE

REQUEST NO.

RESPONDING AGENCY:	CODE:	DATE:	BILL NUMBER:
Office of the State Actuary	035	12/05/01	Tech. Correction

SUMMARY:

Makes technical corrections to the retirement system statutes.

Effective Date: 90 days after session.

BACKGROUND DISCUSSION:

Corrections are required to statutes related to the passage of the retire/rehire bill SB 5937 (2001 2nd sp.s. c. 10) and the funding chapter bill SB 6167 (2001 c 329), and also corrects erroneous cross references in other retirement system statutes.

FISCAL IMPACT:

None.

FISCAL NOTE

REQUEST NO.

RESPONDING AGENCY:	CODE:	DATE:	BILL NUMBER:
Office of the State Actuary	035	12/05/01	Fed. Conform

SUMMARY:

Amends Public Employees' Retirement System Plan 1 and Washington State Patrol Retirement System statutes related to veterans to conform with federal requirements. The Vietnam Era is extended for members who served in the Republic of Vietnam, and prohibitions on military service credit for members in receipt of a full military retirement are removed.

Effective Date: 90 days after session.

MEMBERS IMPACTED:

A small but unknown number of Plan 1 members will have military service qualifying under the provisions of this bill.

FISCAL IMPACT:

Some additional cost will likely result from the changes represented in this bill, though the number of affected members and the amount of service credit is unknown. The provisions of this bill are required by federal law however, and members will receive these benefits regardless of passage.

FISCAL NOTE

REQUEST NO.

RESPONDING AGENCY:	CODE:	DATE:	BILL NUMBER:
Office of the State Actuary	035	12/05/01	PERS 3 Seasonal

SUMMARY:

Members of the Public Employees' Retirement System (PERS) Plan 2 either working in career seasonal positions with an employer or on military leave of absence will have the opportunity to transfer to Plan 3 and receive the additional transfer payment in the event that they are not employed during their employer's transfer window.

Effective Date: 90 days after session.

BACKGROUND DISCUSSION:

The transition period for PERS 2/3 begins on March 1, 2002. Two transfer windows, for each of state government and local government/other PERS Plan 2 members run consecutively. To be eligible for the additional transfer payment, an employed member must both elect to transfer during their transfer period and subsequently earn service credit during February 2003.

Members who are not employed during the transfer window for their employers or February 2003 do not have the opportunity to transfer to Plan 3 and receive the additional transfer payment, though they may transfer to Plan 3 during a subsequent January without the additional payment.

FISCAL IMPACT:

None.

TIAA-CREF

Background:

TIAA-CREF is not a retirement plan but rather a fund sponsor used by higher education institutions to help invest the moneys contributed to member accounts. Higher Education Retirement Plans (HERPs) are Defined Contribution/Annuity plans. These plans are for higher education faculty and select higher education administrators. The element that distinguishes these plans from a pure defined contribution plan is the *Supplemental Benefit*. This benefit guarantees eligible members 50% of their average final compensation upon retirement.

Members of the Washington's HERPs are immediately vested as soon as they begin contributing. However, the supplemental benefit requires a minimum of 10 years of service. The plan is fully portable among all Higher-Ed institutions in Washington. Members are eligible for a service retirement upon termination, but to receive a supplemental benefit, members need to be at least age 62.

There is no single Higher Education Retirement Plan as with PERS or TRS. Each of the 6 colleges and universities administer their own plans, and the State Board for Community and Technical Colleges administers the plan for the State's 30 such institutions.

Committee Activity:

Presentation: TIAA-CREF
November 8, 2001 - Full Committee

Recommendation to Legislature:

None.

Staff Contact:

Robert Wm. Baker - 586-9237 - baker_bo@leg.wa.gov



TIAA-CREF

Robert Wm. Baker
Office of the State Actuary

Joint Committee on Pension Policy
November 8, 2001

Higher Education Retirement Plans

- Defined Contribution / Annuity Plan
- Supplemental benefit
- Higher education faculty and administrators
- Administered by:
 - 6 colleges and universities
 - State Board for Community and Technical Colleges

Plan Features

- Immediate vesting
 - Supplemental requires 10 years
- Fully portable
- Service credit for 5 months (1 semester) and compensation for 70 hours/month
- Service retirement upon termination
 - 10 years and eligible for early retirement under Soc Sec (62)

Contributions

- 5% of compensation prior to age 35
- 7.5% of compensation from age 35
- 10% of compensation at age 50
 - If elected by the member

Traditional TIAA - CREF

- Teachers Insurance and Annuity Association (TIAA)
 - Fixed income investments
- College Retirement Equities Fund (CREF)
 - Equity investments

Other Fund Sponsors

University of Washington Retirement Plan (UWRP)

- Fidelity Investments
- Safeco Mutual Funds
- TIAA – CREF
- The Vanguard Group

Investments

Members may allocate their contributions between various funding vehicles:

- 15 conservative
- 33 moderate
- 25 aggressive

Members may...

- Reallocate or change future contributions
- Transfer existing account balances
- Reallocate funds within the same sponsor

Payouts

- May elect to take 50% of accumulations in a lump sum
- Remainder of accumulations converted to a lifetime annuity in a form offered by TIAA - CREF

Fixed & Variable Dollar Annuities

- TIAA
 - Traditional Annuity (fixed)
 - Real Estate Account (variable)
- CREF
 - Equities (variable)
 - Fixed Income (fixed)
 - Balanced (both)

Supplemental Benefit

Paid if the base pension does not provide a benefit at least equal to 50% of a member's two year average final compensation on retirement date

Eligibility Assumptions

- If married, a Joint and 2/3rds survivor option was chosen
 - If not married, an actuarial equivalent
- Includes all earned benefits
- Contributions were allocated equally between a fixed dollar and variable dollar annuity
- Maximum contributions after age 50

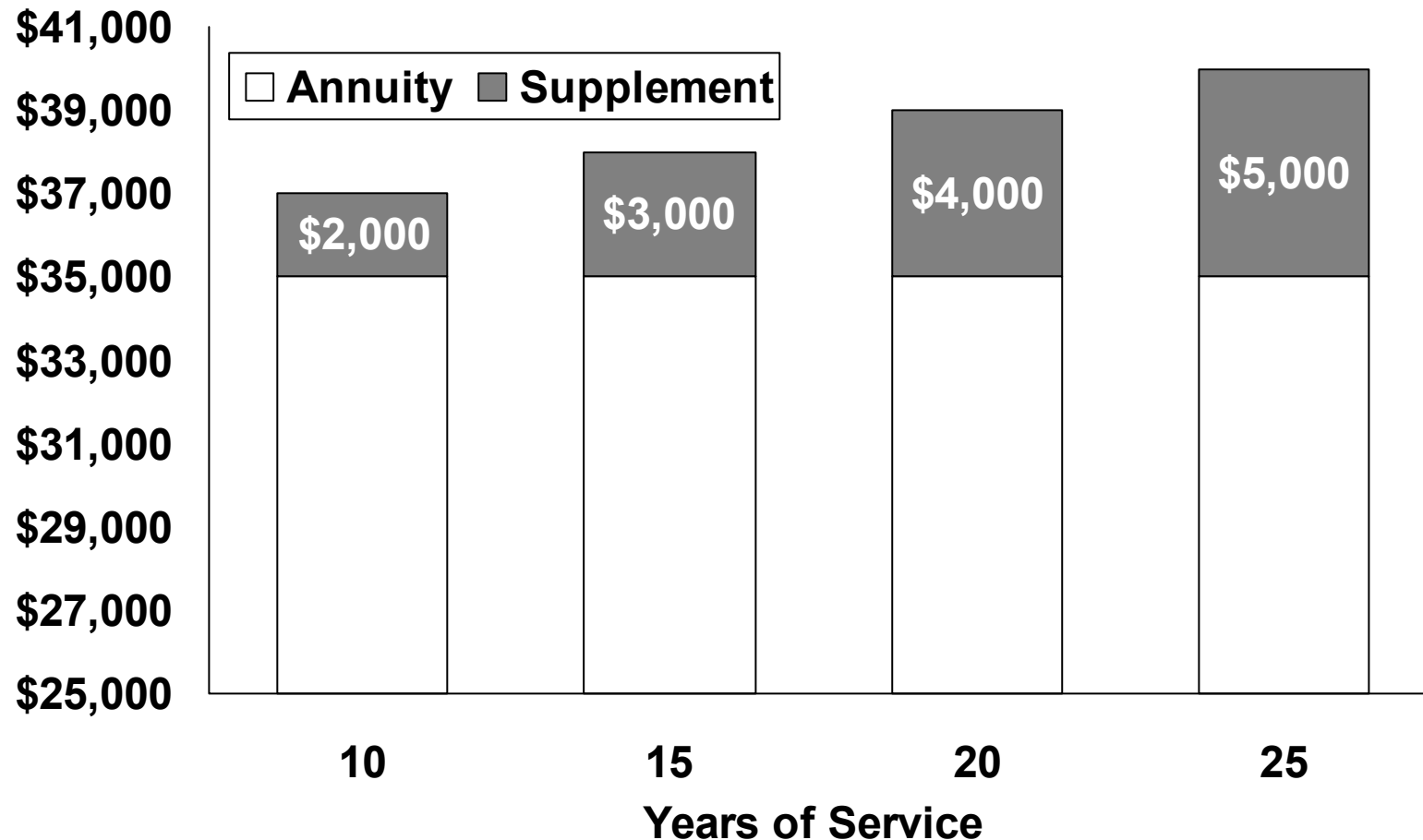
Service Requirement

Members with at least 10, but less than 25 years of service, receive 4% of the full Supplement, multiplied by their Years of Service (YOS).

$$10 \text{ YOS} \times 4\% = 40\%$$

Supplemental Benefit by YOS

**\$80,000 Average Final Compensation (AFC) and
\$35,000 Annuity**

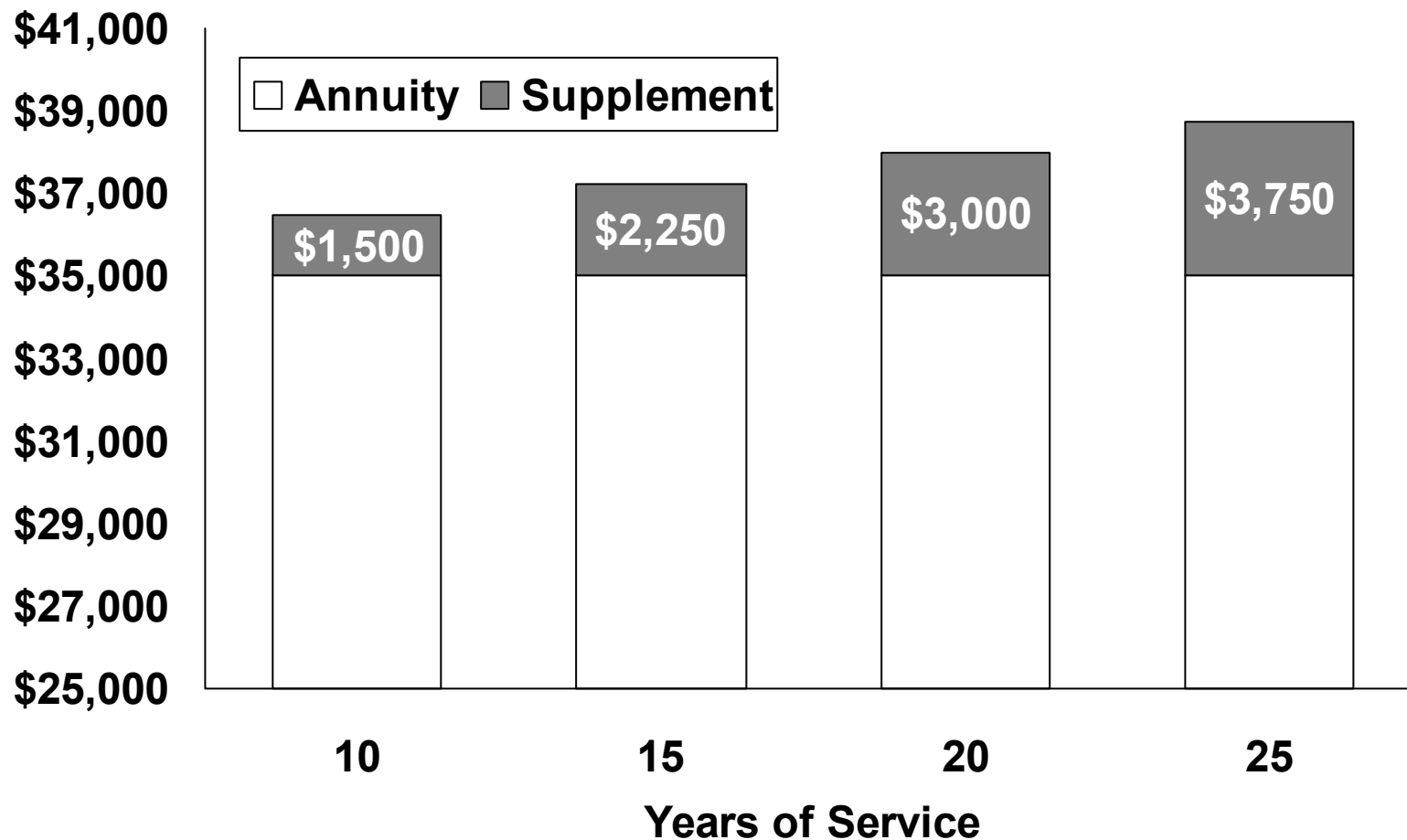


Contribution Requirement

If the member elects to continue contributions at 7.5% after age 50 they are only eligible for 75% of the full Supplement amount.

Supplemental Benefit by YOS

**\$80,000 AFC, \$35,000 Annuity, and
7.5% Contribution Rate (CR)**

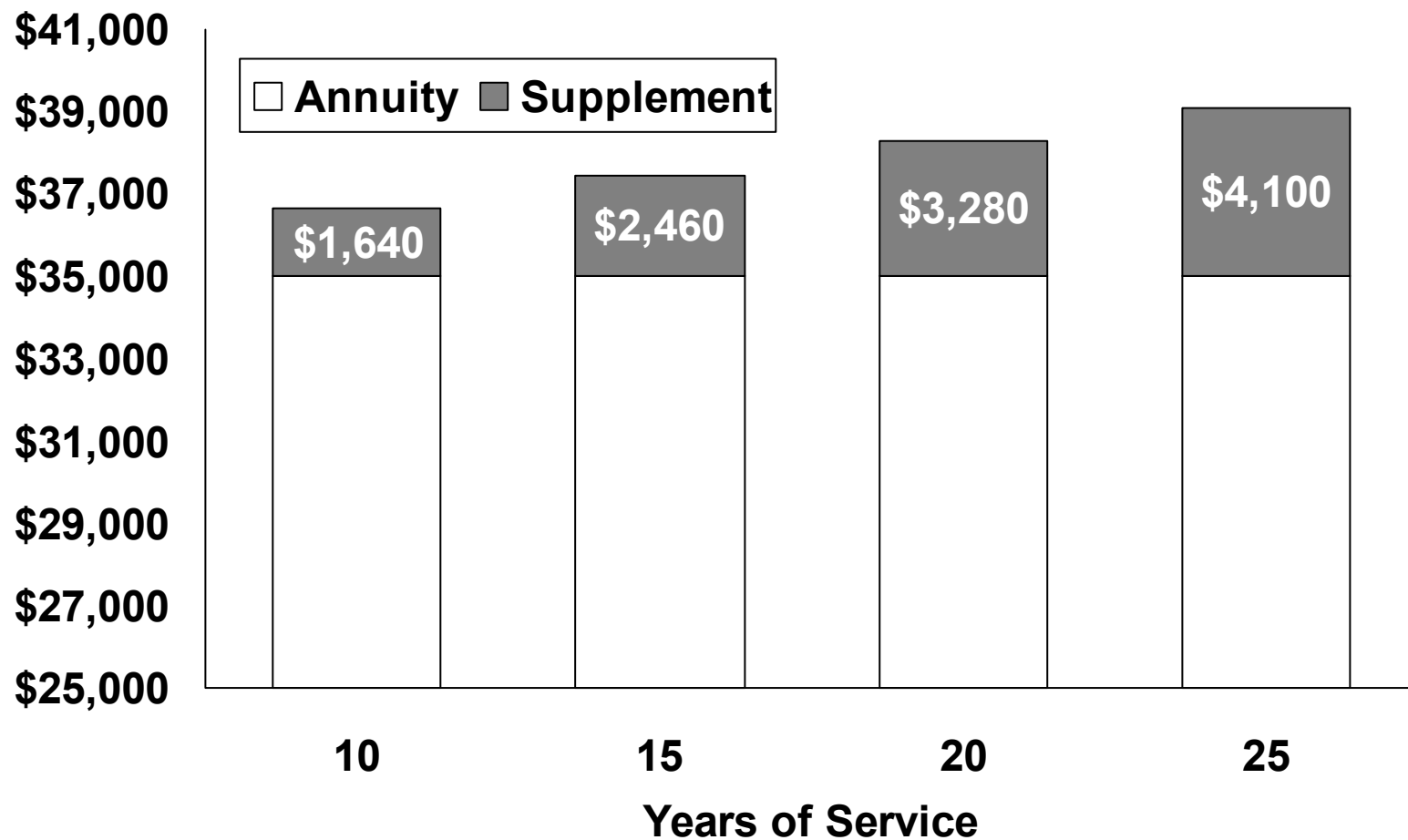


Age Requirement

- Must be 65 to receive full supplement
- Must be 62 to receive a reduced supplement
 - 0.5% / month between age 62 and 65

Supplemental Benefit by YOS

\$80,000 AFC, \$35,000 Annuity, and Age 62

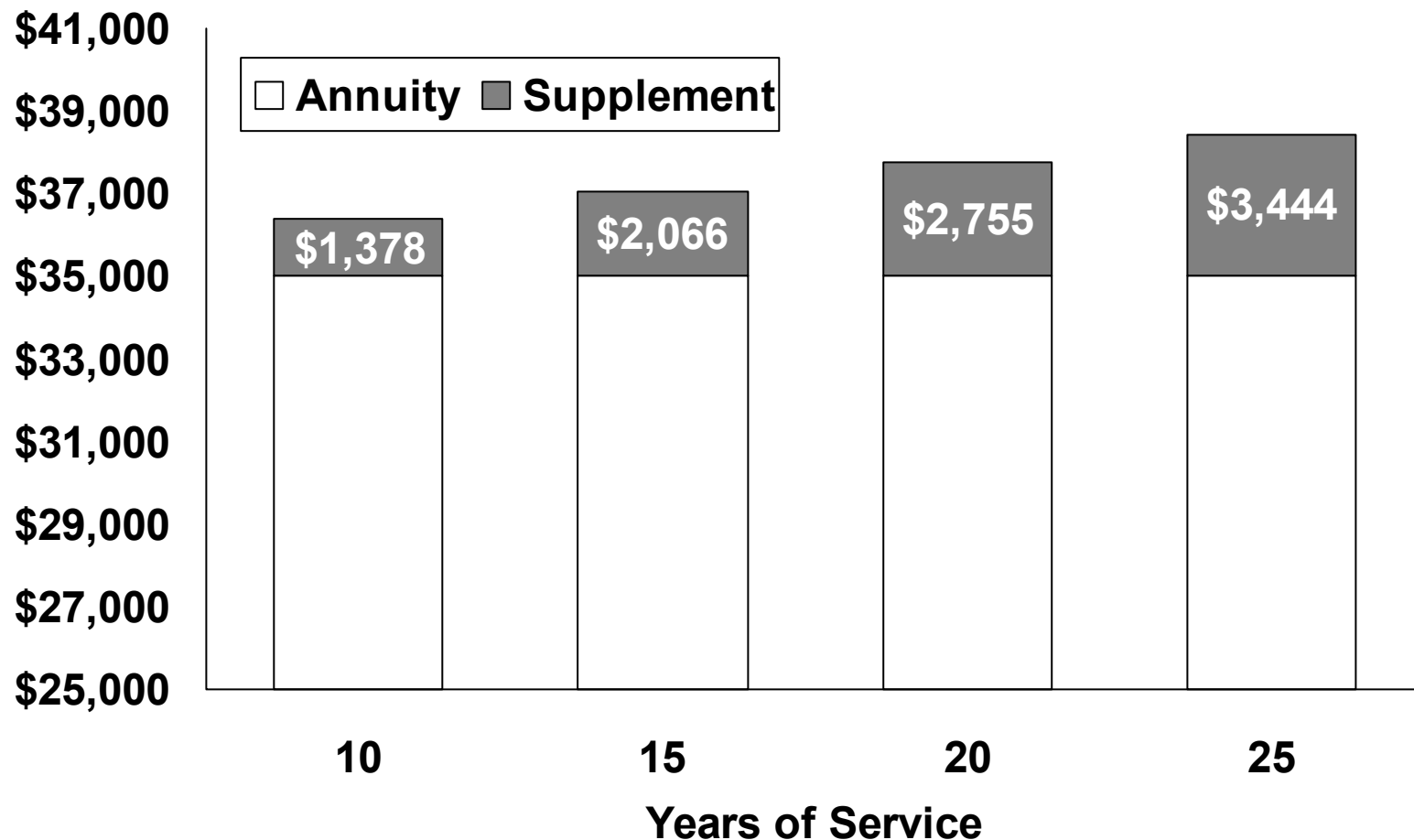


Actuarial Reduction

If a member receiving a supplemental benefit chooses a Joint and Survivor Option, the supplemental amount is actuarially reduced.

Supplemental Benefit by YOS

\$80,000 AFC, \$35,000 Annuity, Age 62, Joint 2/3rds



Disability Retirement

Higher Education Retirement Plan (HERP)

If a member is eligible for a disability retirement, they may receive the supplemental benefit with no reductions on account of age.

Funding the Supplemental Benefit

- Pay-as-you-go
- Paid out of each institution's operating funds

Supplementation Recipients and Cost at Select Institutions

	Number	Annual Cost	Average
CWU	50	\$162,800	\$3,256
EWU	50	\$201,300	\$4,026
WSU	368	\$862,900	\$2,345
UW			

TRS 1 Extended School Year

Background:

Members of the Teachers' Retirement System plan 1 use an average annual salary from their two highest consecutive fiscal years for average final compensation calculations. The fiscal year is defined in TRS plan 1 as running from July 1st to June 31st of the following year. A small number of TRS plan 1 teachers work in extended year schools which extend beyond June 31st. The mismatch of the fiscal year and extended school year could result in a small difference in the TRS plan 1 pension amount.

Committee Activity:

Presentation:

September 11, 2001, Full Committee Meeting

Proposal Approved:

December 10, 2001, Full Committee Meeting

Recommendation to Legislature:

Permit members of the Teachers' Retirement System plan 1 to use two consecutive extended school years, as defined by their school district, in lieu of two consecutive fiscal year in calculating their average final compensation.

Staff Contact:

David Pringle - 586-7616 - pringle_da@leg.wa.gov

TRS 1 Extended School Year

Issue:

Members of the Teachers' Retirement System, plan 1 (TRS plan 1) base their retirement benefit on their years of service credit multiplied by their average earnable compensation in their two highest compensated consecutive years, up to a maximum of sixty percent. Earnable compensation for TRS plan 1 members is defined as all wages paid to the member for services rendered during a fiscal year, which for teachers runs from July 1 to June 30.

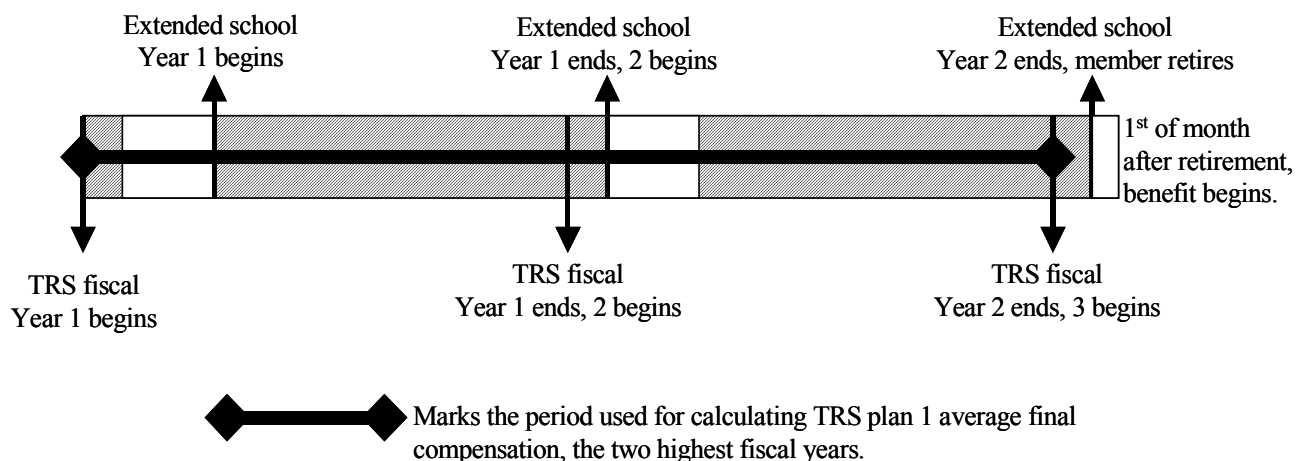
Some teachers work in extended school years which may run until mid July. Recent data supplied by the Superintendent of Public Instruction indicates that about ten school districts have one or more schools that operate on these extended calendars. The difference between the teachers fiscal year and the extended school year may have several effects on TRS plan 1 members benefits.

Analysis:

A. *Extended school year AFC issue*

When members retire in TRS plan 1, RCW 41.32.498 states that their pension allowance shall be equal to their average earnable compensation for their two highest consecutive years of service. RCW 41.32.010(10)(a) specifies that "earnable compensation" is all wages paid for services rendered during the fiscal year.

Illustration of the TRS plan 1 AFC period, Fiscal Year, and an Example Extended School Year



The fiscal year for teachers' runs from July 1st to June 30th of the following year, as set in RCW 41.32.010(12). For teachers that are on a conventional school year schedule, this typically falls in the middle of their summer, as their school year may typically run from late August until mid-June of each year.

A difference in the timing of the end of the statutory fiscal year and the end of the extended school year may result in different earnable compensation amounts for TRS plan 1 members whose annual salary is the same, depending on whether they teach on traditional or extended school-year calendars.

If a TRS plan 1 member retires at the end of an extended school year that runs beyond the end of the fiscal year, the highest two consecutive school years of compensation may not include the final weeks of their career compensation - these fall into a fiscal year during which the member worked only a short period of time.

The Impact of Extended School Year "Look-back" on TRS plan 1 Pension for a typical 2001 retiree

	Conventional School Year		Extended School Year		Difference in Pension amount	
Retirement Date	7/1/01		8/1/01		-	
AFC - using look-back on final two weeks of extended year pay.	\$53,426		\$53,201		\$225 in AFC	
Annual (monthly) pension for 15 years of service	\$16,028	(\$1336)	\$15,961	(\$1330)	\$67	(\$5.60)
Annual (monthly) pension for 30 years of service	\$32,055	(\$2671)	\$31,921	(\$2660)	\$134	(\$11.20)

Instead of these last two weeks, the member includes the two weeks from the "beginning" of the fiscal year - the end of their extended school year - from the year before last. This process of including the weeks taught in the prior school year, but in one of the member's two highest fiscal years that are used for calculating their average final compensation (AFC), is often referred to as the "look-back" process.

As illustrated on the table "The Impact of Extended School Year "Look-back" a teacher who retires" with a typical AFC of about \$53,000 and 30 years of service, the effect of the look-back during years of average salary increases the effect could be to reduce their monthly pension amount by approximately \$11. For a similarly situated teacher with fifteen years of service, that amount would be half, or about \$6.

In plan 2/3 the rules for application and the effective date of retirement negate any difference for teachers on conventional school year calendars or extended school year calendars. This is because the allowance in plan 2 and 3 is calculated on the basis of the "average final compensation" for plan 2 and 3 members, defined as the member's average earnable compensation over the member's highest consecutive sixty service credit months.

This monthly determination in plan 2/3, rather than the annual fiscal year determination in plan 1 effectively eliminates the effects of the extended school year on members of the newer plans.

B. *One Month Later Start to Retirement Benefit - Plan 1*

For a conventional school year TRS 1 teacher that finishes their final contract in mid-June, retirement benefits may begin on July 1st of that year. This is consistent with the rule that benefits begin payment on the first of the month following the month in which the member terminates service. This rule is contained in WAC 415-112-520, interpreting RCW 41.32.480.

Because they retire one month later, teachers similarly situated except for one being in an extended school year program would in a sense receive one less benefit payment during their initial year of retirement. In the above example this amount would be about \$2660 for a teacher with 30 years of service.

In plan 2 and plan 3, a teacher typically does not start their benefit until the September following their retirement, regardless of whether their final school year ends in June or July. The fiscal year definition used in TRS 1 is not used for pensions in the newer plans. A teacher from these plans does not receive service credit for the entire school year, and therefore a reduced benefit, unless their retirement begins at the end of the school year - September through August.

C. *Possible Approach*

TRS plan 1 teachers in extended school year programs could have their average final compensation calculated on the greater of either the current formula of their two highest consecutive fiscal years, or the two highest consecutive extended school years as defined by their school district. This would account for the possible adverse effect of the fiscal year determination on their benefits, but would not address the issue of their benefit starting one month later than conventional school year TRS plan 1 members.

D. *Executive Committee Proposal*

Permit TRS plan 1 teachers in extended school year programs to have either two consecutive fiscal years or two consecutive extended school years, as defined by their school districts, used in the calculation of their average final compensation.

FISCAL NOTE

REQUEST NO.

RESPONDING AGENCY:	CODE:	DATE:	BILL NUMBER:
Office of the State Actuary	035	12/05/01	Z-1154.1/ Z-1155.1

SUMMARY:

Members of the Teachers' Retirement System (TRS), plan 1 teaching in an extended school year program may use two consecutive extended school years, as defined by their school district, rather than two fiscal years in determining their average final compensation.

Effective Date: 90 days after session.

BACKGROUND DISCUSSION:

Some TRS plan 1 members may, under certain circumstances, see a slight reduction in their retirement benefit if teaching in an extended school year program as compared to another similarly situated member teaching in a conventional school year program. This is due to the final extended school year of their teaching career ending after the end of the last full fiscal year of their career.

MEMBERS IMPACTED:

A small number of TRS plan 1 members likely teach in extended school year programs. Some of them may see a small increase in their average final compensation, and resulting retirement benefit, from this option.

FISCAL IMPACT:

None.